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In the Supreme Court of the United States

OCTOBER TERM, 1944.

No. 426

GEORGE A. BALL,
Petitioner,

vs.

H. EARL COOK,
Superintendent of Banks of the State of Ohio in Charge of the Liquidation of The Union Trust Company, Cleveland, Ohio, Trustee,
Respondent.

PETITION FOR WRIT OF CERTIORARI
To the United States Circuit Court of Appeals
For the Seventh Circuit, and
BRIEF IN SUPPORT OF PETITION.

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Respondent.

PETITION FOR WRIT OF CERTIORARI
To the United States Circuit Court of Appeals For the Seventh Circuit.

George A. Ball prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Seventh Circuit entered in this case on July 7, 1944. This judgment affirmed, with some modification, a judgment of the District Court for the Southern District of Indiana, Indianapolis Division, in favor of respondent and against petitioner in the amount of $3,664,616 with interest from June 19, 1943.* Petitioner's petition for a rehearing

* When judgment was entered by the District Court in this case a like judgment in the same amount was entered in another case brought by respondent against George and Frances Ball Foundation involving substantially the same facts and issues. The judgment in each case provided that payment in whole or in part of either judgment would constitute *pro tanto* a payment of the judgment in the other case. The two cases were heard and decided together in the Circuit Court of Appeals. Contemporaneously with the filing of the petition for writ of certiorari in this case a separate but substantially identical petition is being filed by George and Frances Ball Foundation.

was denied by the Circuit Court of Appeals on August 9, 1944.

OPINIONS BELOW.

Neither the opinion of the Circuit Court of Appeals for the Seventh Circuit (printed in the record, R. 3034-3060, 3072-3073) nor the opinion of the District Court (printed in the record, R. 2725-2763, 2900-2919) has yet been reported.

JURISDICTION.

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (U. S. C., Title 28, Section 347a). This petition is being filed before the expiration of three months from July 7, 1944, the date of the judgment of the Circuit Court of Appeals.

STATEMENT OF THE MATTER INVOLVED.

Respondent is the successor in interest to the partnership of O. P. and M. J. Van Sweringen of which O. P. Van Sweringen and M. J. Van Sweringen were the sole partners. For many years Van Sweringens dominated a holding company system which controlled a number of railroads and real estate enterprises.

a. C.T.B. and Vaness Loans.

In 1930 two companies in the Van Sweringen holding company system—The Vaness Company and The Cleveland Terminals Building Company (hereafter called "Vaness" and "C.T.B.")—borrowed respectively $16,000,000 and $23,500,000 from J. P. Morgan & Co., and pledged as collateral various securities including those which represented the controlling link between the top holding companies and the operating companies in Van Sweringens' holding company system. Van Sweringens individually guaranteed payment of each of these loans. Upon maturity of these

loans on May 1, 1935, neither C.T.B. nor Vaness nor Van Sweringens could pay. Van Sweringens, both individually and as a partnership, were insolvent to the extent of many millions of dollars.

At all relevant times Van Sweringens were officers and directors of C.T.B. and Vaness and dominated the affairs of those companies (R. 2843).

b. Van Sweringens' Relationship with J. P. Morgan & Co.

Van Sweringens had very close business relations with J. P. Morgan & Co. and the several banks associated with Morgan in the C.T.B. and Vaness loans. Morgan and associated institutions had headed underwriting groups through which more than $800,000,000 of securities of Van Sweringen companies had been publicly distributed. Morgan and other associates were acting as trustees for approximately $1,000,000,000 of securities of Van Sweringen companies (Finding No. 16, R. 2718).

c. Cleveland Bank Debts of Van Sweringen Partnership.

When the C.T.B. and Vaness notes matured on May 1, 1935, the Van Sweringen partnership owed approximately $15,000,000 to four Cleveland banks on loans made in 1930 and earlier, and these loans were in default. These four Cleveland banks are the beneficiaries of respondent's trust and the real parties in interest in this suit.

The maturity of the C.T.B. and Vaness notes and the consequent necessity of a foreclosure of the pledged collateral threatened Van Sweringens' continued control of their holding company system. For about three months after May 1, 1935, Van Sweringens negotiated with Morgan for a private sale of the collateral and concurrently attempted, without success, to induce their Cleveland bank creditors and others to provide sufficient money to buy the collateral from Morgan (R. 326, 2709).

d. Written agreement between Ball and Van Sweringens.

In August, 1935 Van Sweringens, accompanied by one G. A. Tomlinson, went to Muncie, Indiana to interest petitioner Ball in the purchase of the C.T.B. and Vaness collateral. Ball had had no previous business relationship of consequence with Van Sweringens. They represented to Ball that there was a good investment opportunity in the securities that were about to be sold. After some investigation Ball concluded, together with Tomlinson, to make the investment.

Ball, Tomlinson and Van Sweringens entered into a written agreement which recited that Ball and Tomlinson would be willing to make the investment if Van Sweringens would continue in the management and direction of the various companies involved, and which provided that Ball and Tomlinson would invest $2,015,000 in a corporation (Midamerica Corporation) which would make the purchase —subscribing for 20,000 shares of preferred stock at $100 per share and 15,000 shares of common stock at $1 per share; and that they would grant to Van Sweringens a ten year option to buy 8250 shares (55%) of the common stock for $1 per share at any time after Van Sweringens had paid or adjusted their debts. Ball and Tomlinson subscribed and paid for the agreed amounts of stock. This was the only capital ever invested in Midamerica (R. 2713-2716).

e. Purchase by Midamerica of C.T.B. and Vaness collateral.

Meanwhile Morgan had published notice of the public sale—to be held in New York City on September 30, 1935—of the C.T.B. and Vaness collateral. At the sale Midamerica purchased the collateral essential for the control of the holding company system for $3,121,000, using in payment the capital subscribed by Ball and Tomlinson supplemented by a bank loan.

According to the findings of the District Court, approved by the Circuit Court of Appeals, Van Sweringens

(i) had arranged with Morgan for a grouping of the collateral favorable to the purchase by Midamerica, (ii) had persuaded reluctant associates of Morgan to acquiesce in the arrangements made for the sale, and (iii) by reason of their unusual relationship to Morgan had brought to Midamerica "the opportunity to purchase securities for $3,121,000 which, at the date of purchase, had a far greater value to Midamerica, organized and officered as it was." (R. 2718, 2719.) As already noted, the collateral Midamerica bought had been pledged with Morgan by C.T.B. and Vaness of which Van Sweringens were the dominant directors.

The two Van Sweringens became president and vice-president, respectively, of Midamerica and continued to manage its affairs until their respective deaths. M. J. Van Sweringen died December 14, 1935 and O. P. Van Sweringen November 23, 1936. For their services to Midamerica during the period from September 30, 1935 to November 23, 1936 the Van Sweringens were paid over $133,000 by Midamerica (R. 950, 966).

Both Van Sweringens died insolvent. They did not during their lifetime pay or adjust their debts—which by the terms of the written contract with Ball and Tomlinson was a condition precedent to the exercise of their right to acquire 8250 shares of Midamerica stock.

f. Midland Bank Situation.

Midland Bank of Cleveland (one of respondent's beneficiaries and a real party in interest in this suit) had been a participant with Morgan in the loan to Vaness. Midland had manifested some reluctance to go along with Morgan in the public sale of the collateral (R. 900, 901). It was thereupon arranged by Tomlinson, who was a director of Midland, that whatever Midland got as its share from the foreclosure of the Vaness collateral, it could invest in Midamerica stock on the same terms as he and Ball were in-

vesting, i.e., 55% of the common stock would be subject to the option to Van Sweringens (R. 902-904). Midland's share of Midamerica stock (1006 shares of preferred and 754½ shares of common) was supplied by Tomlinson. At all times before the deaths of Van Sweringens Midland treated its Midamerica common stock (754½ shares) as subject to the option to Van Sweringens "to the extent of 55% thereof" (R. 1390-1392).

After both Van Sweringens had died Ball, Tomlinson and Midland all treated Van Sweringens' interest in Midamerica stock as having terminated (R. 983, 1400).

In December, 1935 Ball agreed to buy all of Tomlinson's Midamerica stock and by April 1, 1937 had acquired most of it. On that date Ball held 14,050 shares which he transferred as a gift to George and Frances Ball Foundation, an Indiana charitable corporation (hereafter called "Foundation").

Later in April, 1937 the Midland Bank made an absolute and unconditional sale—on terms inconsistent with the existence of any rights in Van Sweringens—of all its Midamerica stock to Foundation at a profit of over $500,000. The other three Cleveland banks for whom respondent sues had a financial interest in Midland, and they approved or ratified the sale and benefited from it in the amount of over $380,000.*

g. Claims made by Cleveland Banks and Partnership Receiver.

Shortly after O. P. Van Sweringen's death representatives of two of the Cleveland banks which were credi-

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* Midland was in liquidation under an arrangement by which Cleveland Trust assumed all of Midland's liabilities. Other Cleveland banks agreed to share with Cleveland Trust in designated proportions any loss incurred in this liquidation. At all relevant times it has been clear that the liabilities would exceed the assets. Thus every dollar realized from Midland's assets decreased the ultimate liability of these participating banks.

tors of the Van Sweringen partnership asserted to Ball and Tomlinson a claim that the rights of Van Sweringens under the option continued; and later upon the appointment of a receiver for the Van Sweringen partnership, the receiver likewise asserted a claim to the 8250 shares (R. 981-984). The receiver later sold all of the assets and rights of the partnership to respondent who was to hold them in trust for the four banks in the proportions of their respective claims against the Van Sweringen partnership (R. 726-733).

h. Proceedings in lower Courts.

In September 1939 respondent commenced the present action, and after a hearing the District Court held—substantially in accordance with respondent's contentions—that the agreement between Ball, Tomlinson, and Van Sweringens was in substance that Van Sweringens were to procure a bargain purchase of the C.T.B. and Vaness collateral in return for 55% (8250 shares) of the common stock of Midamerica; that Ball and Tomlinson were to provide all the capital for which they were to get preferred stock and 45% of the common stock of Midamerica; that the option provisions of the written contract between Ball, Tomlinson and Van Sweringens were designed to and did hinder, delay and therefore defraud Van Sweringens' creditors; that Ball held the 8250 shares of common stock as a resulting trustee for the Van Sweringen partnership; that when on April 1, 1937 he transferred to Foundation all the Midamerica stock he held he converted the 8250 shares; and that Ball was liable in damages in the amount of $3,664,616.*

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* After the deaths of both Van Sweringens, C.T.B. and Vaness each sued George and Frances Ball Foundation, Ball and one Bernard claiming that Van Sweringens had violated their fiduciary duties to C.T.B. and Vaness in connection with the purchase of the collateral by Midamerica; that Midamerica was therefore the con-

(*Continued on next page*)

A Special Master to whom a portion of the case was referred found that Van Sweringens, by their activities in connection with the purchase of C.T.B. and Vaness assets by Midamerica, had committed fraud and a breach of fiduciary duty (R. 2847-2849). The District Court confirmed and adopted the finding of breach of fiduciary duty, but not the finding of fraud (R. 2898-2900). The Circuit Court of Appeals also agreed that Van Sweringens had violated their fiduciary duties (R. 3055, 3056).

The Circuit Court of Appeals modified the judgment by holding that Midland Bank's conduct estopped respondent from asserting a claim on its behalf, and reduced the judgment by 55% of the amount paid by Foundation to Midland for the common shares sold to it by Midland (R. 3059, 3060, 3072, 3073). The reduction is less than $400,000.

i. Position of Petitioner.

It is the position of the petitioner that—

(1) The only agreement ever made with Van Sweringens by petitioner was the written agreement under which all that Van Sweringens were to do was to manage Midamerica for which they were to receive (apart from current compensation) a ten year option to buy 8250 shares of Midamerica common at $1 per share exercisable after they had paid or adjusted their debts.

(2) Even if petitioner made the kind of agreement the court below found—which petitioner denies—there can be no recovery, because, under the findings, Van Sweringens

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(*Continued from preceding page*)

structive trustee of the assets purchased; that Ball Foundation and Bernard were participants with Midamerica; and that they should be required to account for any profits received (R. 2723-2724). The C.T.B. and Vaness suits were settled through the payment by Foundation of $662,500; and Ball, Foundation and Bernard received releases from C.T.B. and Vaness (R. 2922-2928). In rendering judgment in the instant case the District Court allowed a credit in the amount of 55% of this $662,500 (R. 2930, 2932).

entered into an arrangement under which they were to procure for Midamerica a bargain purchase of the securities pledged by C.T.B. and Vaness, and in consideration of this they were to receive the 8250 shares of Midamerica common. Respondent was required to prove and rely upon this agreement. The activities of Van Sweringens under this agreement constituted a serious violation of their fiduciary duties as the dominant officers and directors of C.T.B. and Vaness—and the lower courts have so found. The agreement was therefore illegal and contrary to public policy. In consequence, respondent, who must rely on the rights asserted to have accrued to Van Sweringens under this kind of agreement, cannot properly invoke the processes of a federal court to obtain a recovery.

(3) When Midland Bank sold its Midamerica stock to Foundation, Midland (and through Midland the other three banks whom respondent represents) took the identical position which petitioner Ball took when he transferred to Foundation the shares he held, i.e., that all rights of Van Sweringens in respect of Midamerica stock had terminated. Respondent is therefore estopped to assert in this action that that position was wrongful.

QUESTIONS PRESENTED.

1. Where dominant directors and officers of a corporation have made an agreement involving a serious violation of fiduciary duty under which agreement they are to receive certain stock, may the successor in interest of those directors and officers recover for conversion of the stock (by reason of the refusal of the other party to the agreement to turn over the stock pursuant to the agreement) when in order to establish his right to the stock the successor in interest must prove and rely upon such an agreement?

2. Where the four beneficiaries of respondent's trust have taken the position in connection with Midland's sale of

Midamerica stock to Foundation that all rights of Van Sweringens in respect of Midamerica stock had terminated upon their deaths and have derived a very substantial financial benefit from that sale, is respondent thereby estopped to assert against petitioner that Van Sweringens' rights in Midamerica stock had not terminated?

3. Where a person, who has subscribed and paid a large amount of money for the preferred and the common stock of a corporation, gives to an insolvent debtor, in consideration of personal services, an option to buy part of the common stock for a nominal amount after the debtor has become free of debts, is such a contract a fraud upon the insolvent debtor's existing creditors?

REASONS FOR GRANTING THE WRIT.

A. ON THE ILLEGALITY ISSUE.

First. The Court below has rendered a judgment based on a claim which is contrary to public policy under the applicable local decisions, to wit: a claim based on a contract to compensate Van Sweringens for services, the performance of which constituted a serious violation of fiduciary duty by Van Sweringens who were the dominant officers and directors of C.T.B. and Vaness.

Second. The case presents the following important questions of federal law which have not been, but should be, settled by this Court:

(a) Whether a contract involving a serious breach of fiduciary duty by the dominant directors of a corporation whose securities are widely distributed is contrary to the public policy of the United States; and

(b) Whether federal courts in cases where jurisdiction is based solely on diversity of citizenship should enforce a claim which is contrary to the public policy of the United States.

Third. If such a contract is contrary to the public policy of the United States, then the decision of the Court below is in conflict with the decision of this Court in *McMullen v. Hoffman,* 174 U. S. 639.

Fourth. The decision of the Court below is in conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in *In re The Van Sweringen Company,* 119 F. (2d) 231, on substantially the same matter.

B. ON THE ESTOPPEL ISSUE.

The Court below has decided an important question of local law in a way in conflict with the applicable local decisions in that it has held that respondent is not estopped by reason of the conduct of his beneficiaries other than the Midland Bank.

C. ON THE FRAUD OF CREDITORS ISSUE.

The Court below has decided an important question of local law in a way in conflict with the applicable local decisions, to wit: It has held to be in fraud of creditors an agreement under which Van Sweringens were not to have the right to acquire Midamerica stock until they had paid or adjusted their debts.

WHEREFORE petitioner respectfully prays that a writ of certiorari issue to the Circuit Court of Appeals for the Seventh Circuit requiring that Court to certify and send to this Court for its review and determination a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket "No. 8432, H. Earl Cook, Superintendent of Banks of the State of Ohio in Charge of the Liquidation of The Union Trust Company, Cleveland, Ohio, Trustee, vs. George A. Ball," and that the judgment of said Circuit Court of Appeals in said case be reversed by this Court.

Petitioner's brief in support of his petition is annexed hereto.

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Respondent.

BRIEF OF PETITIONER IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

OPINIONS BELOW.

Neither the opinion of the District Court nor the opinion of the Circuit Court of Appeals has yet been reported. The opinion of the Circuit Court of Appeals is printed at pages 3034-3060 and 3072-3073 of the record. The opinion of the District Court is printed at pages 2725-2763 and 2900-2919 of the record.

JURISDICTION.

Judisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (U. S. C. Title 28, Sec. 347 (a)). The judgment of the Circuit Court of Appeals was entered July 7, 1944. The petition for certiorari has been filed within three months of that date.

STATEMENT OF THE CASE.

A statement of the case is set out in the petition for certiorari (*supra* pages 2 to 9) and will not be here repeated.

ASSIGNMENTS OF ERROR.

The Circuit Court of Appeals erred in each of the following particulars:

1. In failing to follow the applicable local decisions which hold a claim like that asserted by respondent to be contrary to public policy and unenforceable, i.e., a claim founded on a serious breach of fiduciary duty by the dominant officers and directors of corporations.
2. In holding that a claim based on the violation of fiduciary duty by dominant officers and directors of a corporation involves no question of public policy.
3. In holding that the illegal agreement here involved has been completed.
4. In holding that petitioner may not assert the defense of illegality.
5. In enforcing a claim which is in violation of federal public policy, i.e., a claim based on a serious violation of fiduciary duty by the dominant officers and directors of corporations.
6. In failing to follow the rule with respect to the enforcement of an illegal contract established by this Court in *McMullen v. Hoffman*, 174 U. S. 639.
7. In failing to apply correctly the applicable principles of quasi-estoppel.
8. In holding that the agreement petitioner and Tomlinson made with Van Sweringens was in fraud of Van Sweringens' creditors.

ARGUMENT.

A. THE JUDGMENT IS BASED UPON A CLAIM WHICH IS CONTRARY TO PUBLIC POLICY.

The judgment in this case is based on a claim which is illegal and condemned by public policy. Respondent, who stands in the position of Van Sweringens, has obtained a judgment on a claim which is essentially for compensation for a serious violation of fiduciary duty. Respondent contended, and the court found, that Van Sweringens made an agreement with petitioner and Tomlinson under which Van Sweringens were to receive 8250 shares of Midamerica common in consideration of their services in obtaining a bargain purchase of the C. T. B. and Vaness collateral at the Morgan sale.*

At all relevant times Van Sweringens were the dominant directors and officers of C. T. B. and Vaness, and, therefore, they violated their fiduciary duties to these companies. *The Special Master, the District Court, and the Circuit Court of Appeals have all recognized that Van Sweringens violated their fiduciary duties. Under well settled principles of public policy, it therefore follows that respondent should have been denied recovery.*

Respondent's evidence was to the effect that the collateral bought by Midamerica had a fair and reasonable market value of more than $2,000,000 in excess of what Midamerica paid (R. 353-355, 395-396). The District Court found that J. P. Morgan & Co. and the associated banks which held the collateral had had close financial relationships with the Van Sweringens, including underwriting of more than $800,000,000 of securities of Van Sweringen companies and trusteeships for more than $1,000,-

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* Petitioner contends that he made no such agreement, and that the only agreement he did make is fully set out in the written agreement of September 21, 1935 (R. 2713), which was entirely valid and proper. The illegality, and the illegal agreement, result from the conclusions of the courts below, which conclusions petitioner challenges (See *infra* pp. 27 to 30).

000,000 of their securities; that during the critical period when the sale of the collateral was being arranged Van Sweringens were in almost daily communication with Morgan and arranged for the grouping of the collateral in a manner which facilitated the purchase by Midamerica; that Van Sweringens "by reason of their unusual relationship to [the Morgan group] and their negotiating skill and business acumen, * * * brought to Midamerica * * * the opportunity to purchase securities for $3,121,000 which, at the date of the purchase, had a far greater value to Midamerica, organized and officered as it was"; that all of the services were rendered on or prior to September 30, 1935, the date of the auction sale; and that for their services Van Sweringens were entitled to 55% of the Midamerica common stock (8250 shares) upon the payment of $1.00 per share (Findings No. 16, No. 17; R. 2718-2720).

Without proof of and reliance upon these services and the agreement, pursuant to which Van Sweringens were to be compensated, plaintiff could not have maintained his case. Furthermore, the record discloses that all of the banks whom respondent represents either participated in the wrongful activities of Van Sweringens, or were familiar with and gave approval to them.*

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* One of respondent's beneficiaries, Midland Bank, as a member of the Morgan Syndicate, had manifested some reluctance to acquiesce in the sale as arranged by Morgan. When Midland was allowed to participate in Midamerica's purchase, Midland acquiesced in the arrangements (R. 900-904). Midland was under the direct supervision of Cleveland Trust (another of respondent's beneficiaries), and a Vice-President of Cleveland Trust acted for Midland in the matter (R. 1408-1410). The executive committee of the Cleveland Trust formally approved Midland's participation in Midamerica (R. 908, 909).

A representative of Union Trust (another of respondent's beneficiaries) testified that a Morgan partner told him in May, 1935 that the price for the C.T.B. and Vaness collateral "would be lower if the deal was worked out to the satisfaction of the

(*Continued on next page*)

The basic question, therefore, is whether respondent—relying upon an agreement and activities involving serious violations of fiduciary duty—may be permitted to use the processes of a federal court to obtain a recovery.

1. The judgment is based upon a claim which is contrary to the public policy under the applicable local decisions.

Jurisdiction of the District Court was based solely on diversity of citizenship. When the defense of illegality was asserted it became the duty of the District Court to determine under the Indiana decisions what law governed the validity of the contract in controversy (*Klaxon Company v. Stentor Electric Manufacturing Company,* 313 U. S. 487). The contract which was given effect by the Court was not the written agreement, and the findings do not disclose the place of the making of the contract which was given effect. Under the evidence it might have been made in Indiana, Ohio, or New York. So far as performance is concerned the performance by Van Sweringens was partly in Ohio, partly in New York and partly by long distance telephone conversations between Ohio and New York. Where the place of performance of a contract and the place of making it differ the Indiana conflicts decisions do not clearly establish which law governs. *The Conflict of Laws,* Beale (1935), Sec. 332.22, pp. 1133-1135. However, it is well established in Indiana that a contract repugnant to the public policy of the forum is unenforceable. *Lake Shore & M. S. Ry. Co. v. Teeters,* 166 Ind.

(*Continued from preceding page*)

Cleveland bank creditors" (R. 267). Another representative of the Union Trust, who was also a spokesman for the Guardian Trust (the fourth of respondent's beneficiaries) testified that a Morgan partner had told him that Morgan "would be willing to make a very low price on the collateral." (R. 303). This same representative of Union and Guardian testified that with respect to the C.T.B. and Vaness collateral "our principal interest was that they be cheap enough" (R. 308).

335, 77 N. E. 599; *Vandalia R. Co. v. Kelly,* 187 Ind. 323, 119 N. E. 257; *Carl Hagenbeck & Great Wallace Show Co. v. Randall,* 75 Ind. App. 417, 126 N. E. 501.

As a practical matter it makes no difference whether the law of Indiana, Ohio, or New York governs the question for there is no significant difference in principle in the applicable decisions in any of these states. As hereafter shown *both lower courts have reached a result in conflict with the local decisions of Indiana, Ohio, and New York.* Under the law of each of these jurisdictions (a) it is a matter of public policy that corporate officers and directors adhere strictly to their fiduciary obligations, (b) agreements in violation of fiduciary relations and obligations are illegal, and (c) when a party in order to establish his claim relies upon and must prove an illegal agreement his claim will not be enforced.

Although the District Court found a breach of fiduciary duty, it did not expressly consider the illegality issue despite the fact that the defense was pleaded and exhaustively briefed. The Circuit Court of Appeals did consider the issue but erroneously held—

(a) that no question of public rights as distinguished from private rights was involved;

(b) that "Van Sweringens' activities, in violation of a fiduciary duty, could only affect the title of Midamerica to the assets purchased * * * [and] could not affect the arrangements between them and Ball as to the ownership of the 8250 shares" (R. 3056), i.e., that despite the breach of fiduciary duty by Van Sweringens, Ball could not assert the resulting illegality as a defense against Van Sweringens' successor in interest, the respondent; and

(c) that the illegal transaction had been consummated.

Each holding is contrary to the applicable local decisions.

(a) *As to the public rights and public policy.*

The Circuit Court of Appeals in distinguishing *McMullen v. Hoffman,* 174 U. S. 639, cited by petitioner on the illegality issue, said that that case had involved collusive bidding on public works and hence affected public rights, but that there are no public rights involved in this case (R. 3054). This is an erroneous conception of the limitations of public policy. Many transactions are contrary to public policy which do not involve collusive bidding on public works, fraudulent use of public funds, or breach of a public trust. *Public policy questions have never been limited to such matters.*

In the present case C.T.B. and Vaness had aggregate debts which exceeded $100,000,000 (R. 1218-1220; 2465-2466). In the case of C.T.B. millions of dollars of securities were widely distributed in the hands of the public. Van Sweringens were the dominant officers and directors of these companies and the only persons purporting to act for them in connection with the Morgan sale—and at the same time they were pursuing their own selfish interests to procure a bargain purchase of the collateral pledged by the companies they pretended to serve. In such circumstances the fidelity and integrity of dominant officers and directors is a serious matter of public concern; and there is an unmistakable public policy against agreements made by persons in position of trust, such as officers or directors of corporations, which involve violations of fiduciary duty. The decisions of Indiana, Ohio and New York establish this proposition.

Typical is the holding of the Supreme Court of Ohio in *Thomas v. Matthews,* 94 Ohio St. 32, 113 N. E. 669:

> "A contract made by a director of a corporation that limits or restricts him in the free exercise of his judgment or discretion, or that places him under direct and powerful inducements to disregard his duties to the corporation, its creditors and other stockholders in the management of corporate affairs, is against public policy and void."

See also *Leader Pub. Co. v. Grant Trust & Savings Co.*, 182 Ind. 651, 661, 108 N. E. 121, 124; *Wayne Pike Co. v. Hammons, et al.*, 129 Ind. 368, 27 N. E. 487; *Schemmel v. Hill*, 91 Ind. App. 373, 385, 169 N. E. 678, 682; *Cleveland, etc. R. Co. v. Pattison*, 15 Ind., 70; *Munson v. Syracuse, etc. R. Co.*, 103 N. Y. 59, 8 N. E. 355; *Globe Woolen Co. v. Utica Gas & Electric Co.*, 224 N. Y. 483, 121 N. E. 378; *Landes v. Hart*, 131 App. Div. 6, 115 N. Y. Supp. 337.

C.T.B. was an Ohio corporation; Vaness a Delaware corporation (R. 639, 643). If the law of the state of incorporation should govern, the Ohio cases cited are apposite; and the Delaware law is to the same effect. *Guth v. Loft, Inc.*, 5 A. 2d, 503, 510.

(b) *As to the right of petitioner to assert the defense of illegality.*

The holding of the Circuit Court of Appeals that Van Sweringens' activities in violation of fiduciary duty could only affect the title of Midamerica to the assets purchased and could not affect the arrangements between Van Sweringens and Ball as to the ownership of the 8250 shares is manifestly erroneous. Wherever a contract is made between A and B which involves a violation of B's duty to C, it is always competent for A in a suit by B to point out the illegal nature of the agreement. Contracts which merely involve a transgression of contractual rights of third parties are illegal and unenforcible between the parties to the contract. (*Jackson v. Bryant*, 33 Ohio App. 468, 169 N. E. 825; *Reiner v. North American Newspaper Alliance*, 259 N. Y. 250, 181 N. E. 561.) *A fortiori* contracts which involve violation of fiduciary duties are illegal and unenforceable. See also *Cleveland, etc. R. Co. v. Pattison*, 15 Ind. 70.

(c) *As to the completion of the illegal transaction.* It is true that the illegal conduct, i.e., the breach of fiduciary duty was completed; but the *illegal agreement*, i.e., to give

the Van Sweringens 55% of the stock, *was not completed* and will not be completed unless the judgment herein becomes final. We recognize that in the law of illegal contracts there is an area in which it is difficult to know whether the illegality is so closely connected with a cause of action as to make it unenforceable. But this case is clearly outside that area.

In *Williston on Contracts,* Rev. Ed. p. 4982, it is said that "*a plaintiff cannot be allowed to recover if as a part of his case he is compelled to allege and prove unlawful acts or bargains* * * *."

Under this test respondent should clearly have been denied recovery. It is difficult to conceive of a more serious breach of fiduciary duty than that disclosed by respondent's evidence to the effect that C.T.B. and Vaness assets were bought for more than two million dollars less than their fair market value and that this bargain was procured directly through Van Sweringens' efforts. Furthermore the crucial findings of the District Court (Findings No. 16, No. 17; R. 2718-2720) when read in the light of the undisputed fact that Van Sweringens were in a fiduciary relation to C.T.B. and Vaness clearly disclose a most serious and reckless violation of fiduciary duty.

The Indiana decisions, the Ohio decisions, and the New York decisions show that whenever a party is required to prove an illegal agreement as a part of his case he cannot succeed. *Overshiner v. Wischart,* 59 Ind. 135; *Western Union Telegraph Co. v. Yopst,* 118 Ind. 248, 20 N. E. 222; *Pagel v. Creasy, et al.,* 6 Ohio App. 199; *King & Co. v. Horton,* 116 Ohio St. 205, 156 N. E. 124; *Reiner v. North American Newspaper Alliance,* 259 N. Y. 250, 181 N. E. 561.

2. The illegality issue presents important questions of public policy which have not been, but should be, settled by this Court.

The existence of a strong local policy condemning the claim on which this judgment is based is clear. No state decision justifies enforcement of such a claim. Apart, however, from this strong local policy, we submit that there is also a federal public policy which should prevent enforcement of plaintiff's claim.

a. *The federal public policy against contracts involving a violation of fiduciary duty by officers and directors of corporations.*

The extension of corporate activities and the distribution of corporate securities through many states make the integrity of the conduct of large business corporations increasingly a matter of grave national concern (*Rogers v. Guaranty Trust Co.*, 288 U. S. 123, 149). The Van Sweringen holding company system was national in scope. The railroads under its control had book values in excess of $2,500,000,000 (R. 2705). Some of the securities involved in the sale were listed on the New York Stock Exchange and were traded in on a nation-wide basis (R. 1543). C.T.B. had outstanding over $80,000,000 of debt. Millions of dollars of bonds and land trust certificates of C.T.B. were widely held by the public. The record indicates that the holders of one issue of C.T.B. bonds resided in Kentucky, Pennsylvania, Colorado, New York, Michigan, Minnesota, Florida, Indiana, Wisconsin and Illinois (R. 2444). The conduct of a corporate business so far flung as that here involved affects the national economy at so many points as definitely to make the integrity and fidelity of its officers and directors a matter of national concern.

In several cases where jurisdiction of the federal courts was not based on diversity of citizenship, this Court has insisted upon scrupulous observance of fiduciary obligations and has condemned any deviation from such duties.

Taylor v. Standard Gas and Electric Co., 306 U. S. 307; *Pepper v. Litton*, 308 U. S. 295; *Securities and Exchange Commission v. Chenery Corporation*, 318 U. S. 80, 85.

If these decisions alone do not establish a compelling public policy on the subject, certainly when they are considered in conjunction with the many congressional declarations of public policy as evidenced by the Securities Act, the Securities and Exchange Act, the Interstate Commerce Act, and the Bankruptcy Act, it is clear that there is a strong federal public policy condemning contracts which involve violation of fiduciary duty.

b. *As to the duty of a federal court to refuse to enforce a claim which is contrary to federal public policy.*

We submit that federal courts, when their jurisdiction is based solely on diversity of citizenship, should hold a claim unenforceable when it is contrary to federal public policy even though the claim might not be contrary to local policy. By this we do not suggest a return to the doctrine of *Swift vs. Tyson*, 16 Pet. 1. Certainly if the public policy of a state holds a contract void, federal courts in cases where jurisdiction is based on diversity of citizenship must follow the state public policy. But even though under the state law a claim might not be against public policy, it is inconsistent with the fundamental integrity of federal courts for them to enforce a claim if it is contrary to a clear and unmistakable federal policy. For example, a "yellow dog" contract might be valid under the law of a particular state (as undoubtedly it is under the law of several of the states); and yet in view of the clear public policy of the United States (as evidenced by the several federal statutes dealing with labor relations) against such contracts and all that they imply, a federal court ought not to render judgments based upon such contracts.

This Court has already impliedly held—in a case where federal jurisdiction was not dependent on diversity of citizenship—that federal public policy requires a federal

court to refuse to enforce certain claims independently of any federal statute which is directly applicable. *Morton Salt Co. v. Suppiger,* 314 U. S. 488.

There has been no express holding by this Court in a case where federal jurisdiction is based solely on diversity of citizenship that a federal court must refuse to enforce a claim which is contrary to the policy of a federal statute or series of statutes. We submit that the questions involved in this proposition should be settled by this Court and that this case presents an opportunity for such settlement.

3. If the contract involved in this case is contrary to the public policy of the United States then the decision of the Court below is in conflict with the decision in McMullen v. Hoffman, 174 U. S. 639.

In Point 1 we showed that the contract on which respondent's judgment is predicated is contrary to the applicable local law, and in Point 2 we showed that the contract is contrary to the public policy of the United States.

From either of these premises it follows that the decision of the Court below is in conflict with *McMullen v. Hoffman,* 174 U. S. 639, wherein it was said—

> "In case where any action is brought in which it is necessary to prove the illegal contract in order to maintain the action, courts will not enforce it, nor will they enforce any alleged rights directly springing from such contract." 174 U. S. 639, 654.

Once the substantive local law has established that a claim is contrary to public policy, it becomes a matter of federal procedural law for a federal court in diversity jurisdiction to withhold its aid. If federal public policy holds an agreement to be illegal it follows from *McMullen v. Hoffman,* that wherever a party must prove and rely upon the agreement his alleged rights springing therefrom may not be enforced. The distinction between this case and *McMullen v. Hoffman* made by the Circuit Court

of Appeals (i.e., that the *McMullen* case involved public rights) is without merit for we have already pointed out there is a clear public policy forbidding contracts in violation of the fiduciary obligations of directors and officers. The principle of *McMullen v. Hoffman* is fully applicable and should be applied here.

4. The decision of the Circuit Court of Appeals is in conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in In Re Van Sweringen Co., 119 Fed. (2d) 231 on substantially the same matter.

Among the C.T.B. and Vaness collateral bought by Midamerica were claims against three companies which were in reorganization under Section 77B of the Bankruptcy Act. After the purchase Midamerica filed proofs of claim against these companies based on the obligations purchased. Van Sweringens were in a fiduciary relation to each of the debtors at the time of the purchase. The debtors resisted Midamerica's claims on the ground that by the purchase Van Sweringens had violated their fiduciary duties and that Midamerica should therefore be allowed only the nominal amounts paid for these obligations (an aggregate of $890 for claims having a face amount of more than $20,000,000). The District Court in Cleveland disallowed the claim except in a nominal amount and the Circuit Court of Appeals for the Sixth Circuit affirmed, holding that by reason of the violation of fiduciary duty by Van Sweringens and Van Sweringens' association with Midamerica, Midamerica was disabled from recovering any more than the nominal amount it had paid for the securities. *In re The Van Sweringen Company,* 119 Fed. (2d) 231. Certiorari was denied by this Court, 314 U. S. 671.

Although that case arose in a manner different from this case the facts involved were substantially the same (except that here the evidence discloses a more serious violation of fiduciary duty than appeared in those cases) and

yet in that case the breach of fiduciary duty prevented Midamerica from recovering any more than the nominal amount it had paid, whereas here the breach of fiduciary duty is the very basis of the judgment amounting to more than $3,000,000.

We recognize that a difference in the result of two identical cases arising in different circuits is permissible, for that is the corollary of the proposition that local law must govern; but here there is no difference in the applicable local law.

B. ESTOPPEL.

The lower courts failed to follow the applicable local decisions on estoppel.

The Circuit Court of Appeals recognized that the doctrine of quasi-estoppel is here applicable, but failed correctly to apply the doctrine under the applicable local decisions. Petitioner was found to have converted the Midamerica stock because—acting in accordance with the plain meaning of the written contract—he treated the stock as his own after the deaths of Van Sweringens. Respondent maintains this suit for the benefit of four Cleveland banks—Midland Bank, Cleveland Trust, Guardian Trust, and Union Trust. Midland owned 754½ shares of Midamerica stock under exactly the terms that Ball held his shares, i.e., subject to whatever rights Van Sweringens had. After the death of Van Sweringens, Midland treated its stock exactly as Ball did, i.e., that it owned the stock outright and accordingly it sold the stock to George and Frances Ball Foundation at a profit of over $500,000. The other three Cleveland banks had an interest in Midland and as a result derived from said sale a financial benefit of approximately $380,000.

All four banks who are respondent's beneficiaries either actively participated in the sale by Midland to Foundation or approved and ratified the transaction and all derived and obtained financial benefit from it.

More than two years later respondent, as the trustee for the four Cleveland banks, brought this suit on a theory totally inconsistent with the position previously taken by these banks in the sale by Midland to Foundation. The unconscionable inconsistency in the position of plaintiff in maintaining this action on behalf of the four Cleveland banks gives rise to a quasi estoppel or an estoppel by election.

The Circuit Court of Appeals recognized the existence of an estoppel and modified the judgment of the District Court by reducing it by 55% of the amount that Midland received for the stock. It purported to apply the doctrine of quasi-estoppel but actually applied a kind of set-off or counterclaim. The applicable local decisions and the overwhelming weight of authority are to the effect that estoppel effects a complete disability of the person estopped. *Maxon v. Lane,* 124 Ind. 592, 24 N. E. 683 (entitled in the Northeastern Reporter *"Strafford v. Lane"*); *Wilmore v. Stetler,* 137 Ind. 127, 36 N. E. 856. The four Cleveland banks for whom respondent maintains his action were equal participants in the sale of Midamerica stock to Foundation and it is unconscionable for respondent to maintain on their behalf the inconsistent claim here made. The Court should therefore have effected a complete estoppel as to all of the Cleveland banks.

C. THE FRAUD OF CREDITORS QUESTION.

In holding the contract of September 21 to be in fraud of the Van Sweringen creditors, the lower court failed to follow applicable local law.

At the time Van Sweringens made the contract of September 21 they were insolvent. Their debts were incurred almost entirely as a result of loans made in 1930 and prior thereto. They had long controlled a holding company system that bore their name. They desired, and their creditors desired, that they continue to do so; but they had

no funds with which to buy the collateral necessary to continue their control. In these circumstances they sought to have their creditors provide the money to make the purchase (including the banks for whom this action was brought). At that time it was estimated the collateral could be acquired for $2,275,000 (Midamerica later paid nearly a million dollars more); nevertheless Van Sweringen creditors, including the banks for whom respondent sues, declined to make the investment (R. 337). As a last resort Van Sweringens came to petitioner Ball, a relative stranger.

Ball, together with Tomlinson, was willing to risk an investment of over two million dollars provided Van Sweringens would continue to manage the properties. Ball and Tomlinson, who were providing all the capital, had no obligation to give Van Sweringens any kind of an interest in Midamerica. They owed no duty to aid Van Sweringen creditors and had no desire to be in business with these creditors. If Ball and Tomlinson had merely hired Van Sweringens to manage the properties without reference to any kind of an interest in Midamerica stock, clearly Van Sweringens' creditors could not have complained. In order to assure themselves of Van Sweringens' continued interest in the enterprise and to give an incentive for good management, Ball and Tomlinson agreed that Van Sweringens might, when they became free of debt, acquire 55% (8250 shares) of the Midamerica common for $8250. Concurrently, however, Van Sweringens were compensated for services to Midamerica in an aggregate amount in excess of $133,000 —or at the rate of nearly $10,000 per month. Certainly such an arrangement cannot be said to have deprived Van Sweringen creditors of any rights to which they were entitled.

All of the direct evidence, including the testimony of respondent's witnesses, some of whom were representatives of respondent's beneficiaries, is to the effect that the written agreement was the only agreement ever made between Ball, Tomlinson and Van Sweringens.

The lower courts found that this agreement was in fraud of the Van Sweringens' creditors. We submit that the record clearly establishes that the written agreement was the only agreement ever made between Ball, Tomlinson and Van Sweringens and that under the applicable Indiana law such an agreement is not in fraud of creditors.

In *Wassam v. Raben*, 45 Ind. App. 221, 90 N. E. 636, the wife of a debtor invested her capital in a business which the debtor managed without any contract for compensation. The profits of the business were far in excess of those anticipated and the debtor took from the business only such sums as were required for his individual family expenses. His purpose in making the arrangements was "to prevent the fruits of his earnings from being diverted * * * to the payment of his creditors." When the trustee in bankruptcy of the debtor attempted to reach the profits of the business the Indiana court held that he could not do so.

If a man may give away his services to prevent the fruits of the business in which he is engaged from reaching his creditors, then certainly he can make an agreement under which he acquires the right to purchase stock after he becomes free of debt—particularly when for his services during the intervening period he is paid $133,000 for less than 14 months.

For the reasons above set forth Petitioner requests that the petition for a writ be granted.

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In the Supreme Court of the United States

OCTOBER TERM, 1944.

No. 426.

GEORGE A. BALL,
Petitioner,

vs.

H. EARL COOK,
Superintendent of Banks of the State of Ohio, in charge of the Liquidation of The Union Trust Company, Cleveland, Ohio, Trustee,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

I.
STATEMENT OF THE CASE.

Petitioner's statement of the case omits many matters material to a consideration of the questions presented. It is also inaccurate in important respects, particularly with reference to the questions actually involved and decided. This will be obvious from an examination of the opinion of the Circuit Court of Appeals (R. 3034), the opinions of the District Court (R. 2725, 2900), and the findings of fact (R. 2703-2724, 2920-2930). A complete restatement is necessary in order to present a clear picture of the entire situation.*

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* This necessity, and the extensive quotations from the opinion of the Circuit Court of Appeals, have made this brief longer than desirable, but we trust the Court will find its convenience is best served thereby.

Origin of Van Sweringen Empire.

Many years prior to the transactions here involved O. P. Van Sweringen and M. J. Van Sweringen, brothers, began the acquisition and management of a number of railroads and real estate enterprises which they controlled principally by and through The Vaness Company and one of its principal subsidiaries The Cleveland Terminals Building Company (hereinafter referred to as Vaness and C.T.B.). Their partnership "O. P. & M. J. Van Sweringen" owned a large majority of the common stock of Vaness, and "the development and management of these properties (popularly referred to as the 'Van Sweringen Empire') was the principal occupation and interest of the Van Sweringens, who never married and who, throughout their adult lives, lived and worked together, * * * " (C. C. A. Opinion R. 3035).

Cleveland Creditors.

In 1930 Vaness was indebted to certain Cleveland banks (beneficiaries of respondent's trust) in the amount of approximately $14,000,000 secured by valuable collateral. In order to obtain the loans from the Morgan syndicates described in petitioner's statement, which were essential in order to meet other large maturing obligations, it was necessary that Vaness free itself and said collateral from said indebtedness. In order to make this possible the Cleveland banks loaned a corresponding amount to the partnership, secured by Vaness common stock, and the partnership *contributed* the proceeds to Vaness which in turn paid off said loans. The collateral so released was a part of the collateral pledged to secure the Morgan loan to Vaness and subsequently sold to Midamerica Corporation at the public auction.

The Cleveland banks were never repaid. After the death of O. P. Van Sweringen in November, 1936, a receiver was appointed for the partnership. With a few

minor exceptions the beneficiaries of respondent's trust constituted all of the partnership creditors. A trust was created with one of respondent's predecessors in office as trustee and all interest of the partnership in the common stock of Midamerica and claims arising in connection therewith was purchased from the receiver. This action was brought to recoup in part the losses sustained by such beneficiaries out of such transactions all of the benefits of which inured directly to Vaness and C.T.B.

Negotiations With Creditors.

For some time prior to the maturity of the Morgan loans it was evident that they could not be paid, and commencing in the fall of 1934 the Van Sweringens continuously negotiated with both the New York and Cleveland creditors with a view to effecting an arrangement to extend the time of payment of or for refunding the Vaness, C.T.B., and partnership obligations. They prepared and submitted numerous plans which in general provided for the organization of a new corporation to acquire all pledged collateral, and the acceptance by the creditors, of various classes of securities which would preserve their relative rights. Such plans also provided that the Van Sweringens would own the new common stock with complete or at least a degree of voting control. When the New York loans matured on May 1, 1935, however, the Morgan syndicates decided to sell the collateral. From then until the end of July, when the New York creditors decided to hold a public auction, the Van Sweringens negotiated with the New York creditors for the purchase of the notes and collateral at private sale and with the Cleveland creditors for an adjustment of their debts.

Plans of Van Sweringens to Insulate Any Interest Acquired in Collateral From Creditors.

For several weeks prior to their initial contact with the petitioner, the Van Sweringens had been considering the possibility of developing a device by which they might insulate from creditors their equity in the Morgan collateral, in the event they could obtain financial backing with which to purchase it. A memorandum discussing the problem was prepared on July 15, 1935, and a tentative plan was drafted by their attorney on August 8, 1935. A similar plan was prepared for and taken by them to their first meeting with Ball three days later. Each of the proposals provided for placing in escrow a majority of the common stock of a new corporation organized to make the purchase, under an option agreement giving the Van Sweringens the right to purchase the same for a nominal consideration, after a settlement or adjustment of their debts to the satisfaction of a certain number of the directors, and to vote the stock in the meantime. (Finding 9, R. 2710.)

Meeting With Ball and Subsequent Arrangements.

On August 11, 1935, the Van Sweringens, accompanied by one G. A. Tomlinson, a mutual friend, met with Ball at Muncie, Indiana. The statement of petitioner, however, that the purpose of the trip was merely to interest Ball in an investment which he ultimately decided to make, and that thereafter a written option agreement was entered into, is far from an adequate description of the transaction embodied in the findings of the District Court, and approved by the Circuit Court of Appeals as fully sustained by the evidence. The arrangement actually found to have been entered into is described in the opinion of the Circuit Court of Appeals in the following language:

"Essentially contained in all of the court's findings are these facts:

1. That the contract was an arrangement assuring to the Van Sweringens that Ball would put up $2,000,000 *to help them acquire,** through the medium of a new corporation, the securities pledged to Morgan which were necessary to *their* continued control of the 'Van Sweringen Empire'.

2. That by the arrangement the parties agreed to enter into a joint venture: Ball and Tomlinson to furnish the necessary funds and receive therefor preferred stock of a par value equal to the funds furnished with five per cent interest thereon, and forty-five per cent of the profits represented by 45% of the common stock of the new corporation; the partnership to make the necessary arrangement and handle the transaction and *keep* fifty-five per cent of any profit *through its ownership of 55% of the common stock.*

3. That the proposed division was satisfactory to the parties, but all recognized that, on account of the debt situation of the Van Sweringens, the outright receipt of their interest might result in its being seized by creditors. The Van Sweringens did not desire this result, and Ball and Tomlinson were willing to join with them in a method by which it was considered that such a result could be avoided.

4. The method in question was devised by the Van Sweringens and prepared by their counsel. It consisted of providing for the putting *of their interest in the form* of an option, on the face of which they could obtain their interest by the payment of a nominal amount after they had paid or adjusted their debts.

5. Notwithstanding *the apparent contingent form of their interest, the partnership received immediately substantially all the incidents of ownership of the stock,* including control of the new corporation.

6. The partnership performed its part of the agreement, its performance constituting the real consideration for *their* 8250 shares of stock, and thereby their interest in the stock was available to their creditors.

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* Italics ours unless otherwise indicated.

7. That the condition precedent to the acquisition of the stock by the Van Sweringens was designed to, and did hinder, delay, and therefore defraud the partnership creditors." (R. 3041, 3042.)

This analysis is fully supported by the findings of the District Court as a whole and particularly by Findings Nos. 9 to 11 inclusive (R. 2710-2712), 14 to 20 inclusive (R. 2716-2721), 25 (R. 2723) and 34 (R. 2929).

Following the first meeting Ball made several trips to Cleveland and conferred with O. P. Van Sweringen and within a few days the details of the arrangement were agreed upon, including the division of the stock, the amount of money to be furnished, the form of the purported option to the Van Sweringens, and the collateral to be bid for. O. P. Van Sweringen by negotiation with Morgan & Co. arranged for the segregation of the collateral to be sold into four groups. Groups 1 and 3 comprised the securities necessary to the operation of the "Empire" which the Van Sweringens and Ball desired to buy, while Groups 2 and 4 included the securities which they were not interested in acquiring. This grouping was favorable to Midamerica, only in that it enabled it to make a single bid for the entire group of assets it desired to acquire without having to bid for other assets not desired, or on individual securities desirable only if the entire group could be purchased within the limits of its financial resources. It was equally advantageous to any other bidder desiring to purchase control of the Empire, and there is no finding nor any evidence that it was disadvantageous to Vaness, C.T.B. or anyone else or that negotiating for such arrangement violated any obligation to C.T.B. or Vaness.

On August 22, 1935, representatives of the New York creditors authorized Morgan to proceed with the sale of the collateral at public auction and to give the sale wide publicity. September 30 was selected as the date and nationwide publicity was given. (Finding 12, R. 2712.)

The Van Sweringens carried on all necessary negotiations and furnished all necessary services, including the organization of Midamerica Corporation by their counsel on September 28, 1935. Neither Ball nor Tomlinson took any part in such negotiations or arrangements and substantially all the expense was paid by the Van Sweringens. Petitioner states that the District Court found that they persuaded reluctant associates of Morgan to acquiesce in the sale. Finding 16 (R. 2719), the only finding relating to any such activities of the Van Sweringens, states that they negotiated with New York Trust Company, one of the New York creditors, and thereby assured and obtained its participation in the sale at the upset prices agreed to by the other creditors. It appears without controversy that at a meeting of the New York banks on July 26, 1935, the New York Trust Company asked whether it could withdraw its portion of the collateral and retain its position. In September O. P. Van Sweringen conferred with a representative of the Trust Company and afterwards wrote a letter stating that such a course would split subsidiaries and ownerships and endanger the possibility of obtaining new money, and urging the Trust Company to join with the other banks. (R. 1670, 1671, 883.) There was no finding that Vaness or C.T.B. were thereby harmed or that any fiduciary obligation to either was violated by such action.

On September 30, 1935, the parties executed the letter agreement dated September 21 and prepared by Van Sweringens' counsel on September 27. In addition to the provisions of this agreement summarized by petitioner, it provided that Ball and Tomlinson would deposit the 8250 shares of common stock in escrow under an option agreement giving the Van Sweringens the right to purchase at "our cost plus 5% interest per annum at any time you shall have satisfied five of the six Directors of such corporation that you (in keeping with your expressed desires) have paid or adjusted any and all claims based upon now exist-

ing commitments or relationships that may now or hereafter become enforceable against you". It also provided that the option should be irrevocable and that during its life the Van Sweringens should have "*the sole and exclusive right to vote and represent such deposited shares.*" The $1 per share "cost" was found to have been "purely nominal". (R. 3040.)

Purchase of Morgan Collateral.

The initial Board of Directors of Midamerica named in said letter agreement was equally divided between representatives of the Van Sweringens and representatives of Ball and Tomlinson. The first meeting was held on the day of the auction sale and the Van Sweringens and their close associates were elected to *all* the offices *until the election of their successors.* Since the maintenance of such equal division of the Board was assured by the right of the Van Sweringens to vote the majority of the stock, the officers so elected were as a practical matter assured of continuance in office and in the management of the corporation. (Finding 18, R. 2720.)

At said meeting O. P. Van Sweringen was authorized to bid for and purchase all or any of the securities in Groups 1 and 3 at *such price as he might determine.* The Van Sweringens dealt directly and openly with Morgan & Co. which itself advised the Cleveland creditors and others that the Van Sweringens would be associated in bidding at the sale.

The sale was conducted and wholly controlled by Morgan under its rights and liens and was in no way either conducted or controlled by the Van Sweringens, Vaness or C.T.B. The Van Sweringens had made every effort and exhausted their own resources and credit to protect their companies and prevent the sale.

Midamerica Subsequent to the Purchase.

M. J. Van Sweringen died in December, 1935, and O. P. Van Sweringen died November 23, 1936. Until the latter date they and their representatives *controlled* the affairs of Midamerica. (Finding 19, R. 2721.) No certificates of stock, either preferred or common, were issued until after the death of O. P. Van Sweringen and of course none were ever deposited in escrow. Ball never requested their issuance and no option was ever executed. The Code of Regulations which Ball claimed prevented exercise of control by the Van Sweringens notwithstanding their voting rights, was not adopted until after their death.

The Conversion of the 8250 Shares of Midamerica Common Stock.

Immediately after the death of O. P. Van Sweringen in November, 1936, representatives of the Union Trust Company and Guardian Trust Company liquidations, as creditors of the Van Sweringen partnership, demanded of Ball and Tomlinson that the Van Sweringens' interests in Midamerica stock be protected and accounted for. Several meetings were held and a written demand was served on Ball and Tomlinson in February, 1937.

Shortly afterward in March, 1937, Ball and members of his family incorporated, under the laws of Indiana, the George and Frances Ball Foundation, and when on April 1, 1937, the receiver of the partnership, whose rights were afterwards acquired by respondent, notified Ball that he owned or had the option to purchase said stock and demanded recognition and protection of his rights, Ball's only response was to transfer 14,050 shares of said common stock to the Foundation, without consideration. The District Court held that both Ball and the Foundation thereby became liable for damages for conversion.

Midland Bank Situation.

Tomlinson was a director of The Midland Bank and arranged to permit it to participate to a small extent in his position in Midamerica. There is, however, no evidence that, in the subsequent purchase of Tomlinson's common stock by Ball at the nominal price of $1.00 per share, any agreement was entered into by which Ball acquired the right to call on Midland to supply any part of the Van Sweringen stock. After the death of O. P. Van Sweringen, on instructions of Ball and Tomlinson, a certificate for 5,000 shares of common stock was issued to Tomlinson and 754½ shares thereof were transferred to, and a certificate therefor was unconditionally delivered to, Midland. Midland's records thereafter no longer indicated that the stock was subject to an option but there is no evidence and no finding that Ball ever saw Midland's books or was led to believe by Midland or anyone else that the claim of the partnership receiver was to be abandoned.

On April 24, 1937, Foundation sold a major portion of the common stock and assets of Midamerica for $6,375,000. On April 29, it purchased the preferred and common stock of Midland for $524,000 more than Midland's investment. No reference was made in the negotiations or sale to any obligation of either party to the receiver of the Van Sweringen partnership. Midland was not asked to make any guaranty as to the extent of the interest purchased or the legal effect of its original agreement with Tomlinson. (R. 1379.) It merely accepted the offer and transferred the stock. The District Court made but one finding with reference to the effect of this sale (Finding 34-A, R. 2929) which was that Ball knew all the facts and was not influenced in any manner by any representation or act as to the ownership of the stock by Midland, and was not injured in any manner by the purchase. The demand of the partnership receiver had been made only a month before and the conversion had already taken place. There was no reason

for anyone to believe that the claim was being abandoned and Ball made no such contention.

Foundation had no assets except the proceeds of Midamerica common stock including the converted shares *and the payment to Midland was made from such proceeds.*

Midland had been in liquidation since 1932 under an agreement by which Cleveland Trust Company as liquidating agent took over its assets and assumed its liabilities. Other Cleveland banks including Union Trust Company and Guardian Trust Company had entered into an agreement to absorb a portion of any deficiency of assets under liabilities. At the time of the sale to Foundation however, both institutions were in liquidation in charge of state officers who were then asserting that the agreements were *ultra vires* and void. The most that can be said as to the position of the liquidators is that they made no objection to the sale. They took no action with reference to it and indeed under their contract had no control over the disposition of Midland assets. Long after this case had been tried and while objections to the Master's report were pending a compromise of any liability under said agreements was effected. The sale by Midland, of course increased its assets, and thereby reduced the ultimate claim against Guardian and Union. This is the benefit on account of which petitioner seeks to be freed of his entire liability on the doctrine of quasi estoppel.

The District Court found no ground for the application of any principle of estoppel. The Circuit Court of Appeals held that the doctrine of quasi estoppel by election applied but that, since whatever benefit any of the banks received was at most only a return of a small part of their own money to which they were legally entitled in any event, a proper result was reached by deducting from the recovery 55% of the amount paid by Foundation for Midland's common stock.

The Contention of a Bargain Purchase.

Petitioner states that the District Court held that the agreement was in substance that Van Sweringens were to procure a bargain purchase of the collateral as consideration for their interest in Midamerica and seeks to build his contention of illegality on this premise. There was in fact no such finding. Petitioner bases his assertion on Finding 16 (R. 2719) which states that "by reason of their unusual relationship to the New York creditors and the New York Collateral, and their negotiating skill and business acumen, they brought to Midamerica and to the defendant and Tomlinson the opportunity to purchase securities for $3,121,000 which at the date of purchase, had a far greater value *to Midamerica organized and officered as it was.*"

This is not a finding, and the District Court did not find, that the collateral had a higher market value than the price paid, or that there was any agreement that the interest of the Van Sweringens in Midamerica common stock should depend on obtaining it at a bargain price. The finding plainly refers to a potential value because of the Van Sweringen association, as clearly shown by the following language in the District Court's opinion:

> "The mere fact that the publicity was given to the sale of the securities included in Groups 1 and 3 and that such sale was public, does not necessarily, mean that the price paid was the full value of such securities *to the purchaser.* Neither does it mean that the Van Sweringens contributed nothing of value to the Midamerica Corporation in the purchase of such securities. The character of the securities, the fact that the common stock of Alleghany Corporation sold at the sale was sufficient to guarantee the continued management and control of the vast railroad empire as a going concern, and the further fact that such management and control were to continue in the Van Sweringens—experienced and successful railroad executives—may well be considered in determining the value of such

groups of securities to the Midamerica Corporation. Without these items of value, the groups might well have a less value to other prospective purchasers." (R. 2752, 2753.)

There was neither any evidence, nor any finding that any better bid was obtainable at the sale, or that the price was lower than it would have been otherwise on account of some secret understanding with the New York creditors. Such a contention has twice been before other courts and has been twice rejected.

In *Gochenour v. Morgan & Co.* (C. C. A. 6), 111 F. 2d 378, 385, where the validity of the sale was directly attacked on the ground that the price was inadequate and that there was a secret agreement by Morgan & Co. to prevent competitive bidding, the court in holding that there was no evidence to support such a contention said:

> "Participants were faced with such huge losses on both loans it is unthinkable that they would have abandoned any conceivable value in the securities they had held, for the uncertain benefits of an unsecured claim against a bankrupt estate."

In *Litwin v. Allen* (N. Y. App. Div.), 25 N. Y. S. 2d 667, involving charges of a similar character against the directors of one of the New York banks, the court reached a similar conclusion.

While the respondent introduced some evidence of a higher market value, petitioner introduced evidence to the contrary. (R. 609-611.) Respondent also introduced evidence that the stock had a value at the time of the conversion of approximately twice the value found by the Master. (R. 1808.) Obviously the question of what evidence was introduced is of no consequence except to the extent that it was embodied in some finding of the District Court.

There is no question but what the findings are supported by the great mass of evidence.

II.

QUESTIONS PRESENTED.

The judgment in this case is for the conversion of common shares of Midamerica *which were owned by the Van Sweringens from the time of the organization of Midamerica in September 1935 and which never belonged to Ball or Tomlinson.* (R. 2724, 2929.)

Petitioner states that he accepts the findings of fact made by the District Court and now confirmed by the Circuit Court of Appeals after a careful review of the record (R. 3060), but his appeals and arguments to this Court are not consistent with such acceptance.

Inherent in practically every phase of petitioner's "Position," "Questions Presented," "Reasons for Granting the Writ," "Assignments of Error," and "Argument" are:

> (1) A fictitious conception of the facts as disclosed by the record and found by both courts; and
>
> (2) Fictitious issues of law based upon and sought to be supported by such fictitious conception of the facts.

In the lower court petitioner insisted that Ball and Tomlinson organized Midamerica, owned all of its stock, and as such owners made a gift to the Van Sweringens of an option (conditioned against creditors) on 55% *of their own shares.*

When practically every piece of evidence in the record, including Ball's own testimony, had demonstrated the absurdity of such a position, and the court had found that the Van Sweringens owned 55% of Midamerica common from the inception of the company and that such shares had never been owned by Ball or Tomlinson, petitioner still retained and asserted and continues to assert here all of his technical legal arguments which had been based on his untenable factual position.

He is also continuing here his misconception of the recovery awarded (for the conversion of property belonging to the Van Sweringens) as *a recovery on a contract* whereby Ball and Tomlinson had agreed to give the Van Sweringens stock *which belonged to them* in consideration of the Van Sweringens' agreement to violate their fiduciary duties to their companies.

As clearly demonstrated by the record and found by both courts:

1. The shares in question were never owned by either Ball or Tomlinson but were owned by the Van Sweringens from the inception of Midamerica;

2. By no provision of the preliminary joint venture agreement for the organization of Midamerica did the Van Sweringens agree to perform any illegal act or violate their fiduciary duties; and

3. The recovery awarded was not *on* such a contract, or for agreed pay for illegal acts, or for the delivery of shares which had ever belonged to Ball.

At the foundation of, and inherent in, practically every issue which petitioner asks this Court to review are one or all of these fictitious factual conceptions.

The Circuit Court of Appeals carefully considered and thoroughly disposed of the collateral legal issues thus raised, but its opinion clearly demonstrates that the only real issue is the factual one as to which the findings and judgment of the District Court were fully sustained.

At the outset of its opinion, the Circuit Court said (R. 3035):

> *"The decision turns principally on the question whether the Van Sweringen partnership owned the 8250 shares of common stock of Midamerica Corporation."*

Again (R. 3044):

> "We now consider the all important question in the case: Did the Van Sweringens own the 8250 shares?"

The District Court found that the shares in question never belonged to Ball or Tomlinson and "were the absolute property of the partnership at all times and were held in trust for it * * *." (R. 2929.)

The false nature of the premise of petitioner's contentions on the illegality and related issues is demonstrated by the following from the Circuit Court of Appeals' opinion. (R. 3054, 3055):

> *"Moreover, if we were to accept defendants' contention, we would have to repudiate the basic findings of the court.* We would have to say that Ball and Tomlinson owned all of the common stock of Midamerica outright and merely gave the Van Sweringens a conditional option on it for their agreement to render illegal services, so that recovery herein is enforcing such an illegal contract contrary to public policy. *But the court did not so find.* As we have already stated, the court found as facts, that the parties had entered into a joint venture in which Ball and Tomlinson were to receive forty-five per cent of the profits represented by 45% of the stock of Midamerica, the partnership to receive fifty-five per cent of the profits through its ownership of 55% of the stock; that the partnership performed its part of the agreement, its performance constituting the consideration for their 8250 shares and thereby their interest in the stock was available to them. Thus, the Van Sweringens, not Ball, owned the 8250 shares. The purpose of the arrangement was fully closed, completed and had come to an end."

While we will discuss under "Argument" the various specific points advanced by petitioner, the relationship of these factual misconceptions should be constantly kept in mind for their bearing on the importance and application of each argument.

III.

ARGUMENT.

A. THE FRAUD OF CREDITORS' QUESTION.

Petitioner contends that the District Court and the Circuit Court of Appeals failed to follow applicable local law in holding that the restrictions against creditors in the agreement between O. P. & M. J. Van Sweringen and Ball and Tomlinson were invalid as in fraud of the Van Sweringens' creditors. It is said that this holding is in conflict with *Wasson v. Raben*, 45 Ind. App. 221.* That case merely holds that a husband does not defraud his creditors by giving his services to his wife without compensation. There is, of course, not the slightest indication in the record that the Van Sweringens intended to give their services, without compensation, to Ball or any one else.

Petitioner's arguments in this connection are also based upon his old false premise that the agreement was one by which Ball and Tomlinson were hiring the Van Sweringens to work for a company owned by them by agreeing to permit the Van Sweringens, when they were free from debt, to acquire from them the controlling interest in the enterprise for the nominal sum of $8250.

It is clear from the summary of the District Court's findings of fact, set forth in the opinion of the Circuit Court of Appeals, and herein quoted (*ante* pp. 4-6), that such was not the arrangement between the parties. Rather the arrangement was one for a joint venture, which was consummated about September 30, 1935, and pursuant to which the Van Sweringens, not Ball, became the owners of the

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* The holding in this case is substantially the same as that in *Most Worshipful Grand Lodge v. Allen*, 208 Ala. 29, 94 So. 343, which was cited by the petitioner in his reply brief filed in the Circuit Court of Appeals. The quotation from the opinion of the Circuit Court of Appeals hereinafter set forth conclusively demonstrates the inapplicability of the holding in the *Grand Lodge* case to the case at bar.

8250 shares. There was no provision that they would work for any one. They were working for themselves as the owners of the controlling equity.

In disposing of substantially the same arguments as here made by petitioner, the Circuit Court of Appeals took cognizance of the real nature of the transaction as established by the evidence and soundly and properly applied the applicable local and federal law to the actual facts as found,—saying (R. 3045 *et seq.*):

> "In their reply brief defendants make the further argument that because a creditor has no right to direct a debtor in the disposition of his services, the debtor may give away his services as a gratuity without violating the rights of his creditors. *Most Worshipful Grand Lodge v. Allen*, 94 So. 343.
>
> "To render a contract illegal it is not necessary that a debtor should intend to defraud his creditors in the collection of their claims. It is illegal if made with intent to hinder and delay creditors. *Shapiro v. Wilgus*, 287 U. S. 348, 354. Creditors are entitled not only to be paid, but to be paid as their claims accrue, and a debtor has no more right to postpone payment simply for his own advantage than to defeat it altogether. A purpose to hinder and delay a creditor is, therefore, fraudulent, although the debtor may honestly intend that all his debts shall ultimately be paid, *McBryan v. Trowbridge*, 84 N. W. 1084, 1086.
>
> "The character of an instrument depends upon its effect, since courts look to the real nature of an agreement and not at all upon what the parties call it, *Corbett v. Riddle*, 209 Fed. 811; *Burroughs Adding Mach. Co. v. Bogdon*, 9 F. 2d 54, and an agreement in form a mere option may be held, by reason of the interest in the subject matter of the one holding the apparent option right, to create a present subsisting interest in the property. *Hoover v. Bouffleur*, 133 Pac. 602; *Keeline v. Clark*, 106 N. W. 257 * * *.
>
> "In our opinion the disposition of this case does not depend upon whether the Van Sweringens had a right to give their services to Ball or Midamerica, and it may

be decided without reference to what was said in the *Grand Lodge* case, *supra*. We doubt the applicability of that case, but are certain it is not controlling here.

"The argument that the partnership had no ownership interest in the pledged collateral, begs the question. Plaintiff's claim is not predicated on any property interest of the Van Sweringen partnership in the collateral sold by Morgan. *The real question is whether the partnership was contracting to render their services and relationships in connection with an enterprise, a joint venture, having as its object the acquisition of the collateral, and whether by rendering those services the Van Sweringens acquired property to which their creditors were entitled. Here, according to the findings of the trial judge, sustained by the evidence, which we must accept, the parties entered into a joint venture, the profits of which were to be divided, as already noted, the Van Sweringens' share, because of their debt situation, to be placed in the form of an option. Under such circumstances we think the Van Sweringens acquired property which was available to their creditors* * * *.

"* * * The effect of the court's finding was that the contract was a device resorted to by Ball and the Van Sweringens to hinder, delay, and defraud their creditors. Under such a record we believe the device, designed to cover up the fraud, was a nullity, and the law looks upon the contract as if it had never been executed. Such a contract can never be justified or sanctified by any new shape or by forms or recitals. This principle is as old as the law of morals. *Booth v. Bunce*, 33 N. Y. 139."

Obviously the question of whether a debtor can defraud creditors by giving away his services is an entirely different question from whether he can validly arrange for the fruits of his services when earned, to be put in a form where they cannot be reached by his creditors, especially where, as here, he enjoys all the substantial incidents of ownership in the meantime.

A sound analogy is found in the cases relating to the right to establish spendthrift trusts with the interests of

the beneficiary free from creditors' claims. In most jurisdictions persons may create such trusts as gifts for the benefit of others. But if a person creates, or furnishes the consideration for the creation of, such a trust directly or indirectly for his own benefit the restrictions against creditors are invalid. In such transactions intent to defraud is immaterial. The applicable principles are stated in the *Restatement of the Law of Trusts,* Section 156, as follows:

"*Where the Settlor is a Beneficiary.*

"(1) Where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.

Comment:

* * * * *

"d. *When beneficiary is settlor.* In order that a trust shall come within the terms of this Section it is not necessary that the beneficiary shall have himself conveyed the property held in trust. It is sufficient that he paid the purchase price for a conveyance upon a trust, of which he is the beneficiary or one of the beneficiaries.

* * * * *

"If a person contests a will and in order to settle the contest a spendthrift trust is created in his favor, he has given consideration in agreeing to the settlement made, and the trust created is within the rule of this Section."

The following decisions, among others, support the rule stated:

De Rousse v. Williams, 181 Ia. 379, 164 N. W. 896;
McColgan v. Magee, Inc., 172 Cal. 182, 155 Pac. 995;
Bank of Commerce v. Williams, 96 Mo. 459, 10 S. W. 38.

There is nothing in *Wasson v. Raben, supra,* or in any other Indiana case to indicate that the Indiana courts would reach a result different from that reached here.

B. ILLEGALITY AND PUBLIC POLICY.

The gist of petitioner's argument here is that the courts below,—

(a) condoned a breach of fiduciary duty by the Van Sweringens, and

(b) improperly used the court's powers to enforce an illegal contract, or to assist in the recovery of agreed pay for illegal services,

contrary to public policy and the decisions of this Court and of the local courts.

Petitioner cites no passage from any opinion of the lower courts supporting such contentions.

True, the Circuit Court of Appeals did say (R. 3054):

> "The arrangement pertained to the purchase of property at a public sale which had been widely advertised with a view to selling the securities at the highest possible price. The Van Sweringens, as officers of Vaness and CTB, did not initiate the sale. They could not have prevented it. They had no control over it. *They bid to the limit of the financial backing that they were able to secure. Their bid was the highest.*"

It might be added that they dealt openly and directly with Morgan & Co., who were obviously competent to, and did solely, represent the lien creditors who received every dollar of the proceeds; and that, by reason of their personal guarantee of the loans involved, the Van Sweringens had a special and peculiar right under the authorities to bid at the Morgan sale. 3 *Fletcher, Corporations*, pp. 191, 192; *Tiffany v. Smith*, 124 N. Y. S. 85; *Saltmarsh v. Spaulding*, 147 Mass. 224; *Wabash Ry. Co. v. Iowa & S. W. Ry. Co.*, 200 Iowa 384.

The court did, however, recognize the Van Sweringens' fiduciary obligation, saying (R. 3055):

> "True enough, the Van Sweringens, who dominated Vaness and CTB, owed to those companies a fiduciary duty in connection with the sale of the collateral pledged with Morgan. Although there was no fraud,

it would seem that they did not fully discharge their fiduciary duty."

And the lower courts did give effect to such findings by taking from respondent (through reduction in the recovery) his share of the settlement payments made to Vaness and C.T.B.

Any possible breach of fiduciary duty was thus hardly condoned.

The argument that the recovery granted is for agreed pay for illegal acts is again based throughout on petitioner's persistent misconception of the actual facts as disclosed by the record and findings.

There was no agreement by the Van Sweringens to render illegal services for anyone and no agreement by Ball to pay over something he owned as compensation for such acts. The recovery is of damages for conversion of shares which belonged to the Van Sweringens from the inception of Midamerica and which never belonged to Ball or Tomlinson.

The Cleveland creditor banks (beneficiaries of respondent's trust) loaned the Van Sweringens (largely on the security of Vaness common stock) the $14,000,000 which they contributed to Vaness capital in 1930 and which, with their personal guarantee of the Morgan loans, kept Vaness and C.T.B. afloat during the worst years of the depression. The Van Sweringens exhausted their personal resources and credit in their efforts to save these companies and died owing many millions of obligations incurred in these efforts.

The petitioner converted to his own use and transferred to the Foundation which bears his name, the Van Sweringens' stock in Midamerica,—the only substantial asset to which the Cleveland banks could look for some recovery on their loans to the Van Sweringens made for the benefit of Vaness and C.T.B.

We submit that no public policy of any jurisdiction can possibly sustain the efforts of petitioner to retain the fruits of his conversion by his plea that he personally hired the Van Sweringens (with stock which the courts have found he never owned) to defraud their own companies for his benefit.

The lower courts have not condoned any illegal acts nor have they permitted their offices to be used to enforce an illegal contract or any agreement to pay for illegal acts. They have merely held that, from the inception of Midamerica, the Van Sweringens were the owners of the 8250 shares of its common stock; that, even though, in acquiring such ownership, they may have performed acts involving a technical breach of their fiduciary obligations to their companies, but not fraud or bad faith, such shares were not outlawed from their creditors; and that the conversion of such shares is not to be condoned in one who first joined in the effort to hide them out from such creditors and now, to protect the fruits of his conversion, claims that he employed the Van Sweringens to breach their fiduciary obligations and agreed to pay them for such breach with such shares.

These holdings are not inconsistent with any applicable local or federal cases. They are wholly consistent with the long line of decisions of this Court from *Brooks v. Martin*, 69 U. S. 70 (1863) to *Loughran v. Loughran*, 292 U. S. 216 (1933), which were carefully considered and soundly applied by the lower courts to this case.

1. The Decision is Not in Conflict with McMullen v. Hoffman, but is in Accord with Applicable Local and Federal Law.

The Circuit Court of Appeals properly distinguished the decision of *McMullen v. Hoffman*, 174 U. S. 639. Its discussion of that case is as follows:

> "Defendants' next contention is that plaintiff's claim is unenforceable because it is based on the right

of Van Sweringens to compensation for services which were found to be violative of their fiduciary duties, and they argue that no one claiming through the Van Sweringens can properly be awarded compensation for such services.

"In support of their contention, defendants rely principally upon the case of *McMullen v. Hoffman*, 174 U. S. 639. In that case McMullen sought an accounting of profits claimed to have been made by the defendant upon a contract for the construction of a pipe line, basing his right thereto upon a contract between himself and the defendant, by which they agreed to make separate bids on the pipe line. The bids were not to be in reality competitive. It was agreed that whoever got the contract would permit the other to share in the profits. No disclosure was made to the parties for whom the pipe line was to be constructed that McMullen and the defendant had such an arrangement.

"In denying recovery the court said:

> 'In case any action is brought in which it is necessary to prove the illegal contract in order to maintain the action, courts will not enforce it, nor will they enforce any alleged rights directly springing from such contract.' p. 654.

"Hence defendants argue that since plaintiff's claim is unenforceable, as a matter of public policy, they should be allowed to retain the full benefits of their conversion.

"A person does not become an outlaw and lose all rights by doing an illegal act. Courts grant relief against present wrongs and enforce existing rights, although the property involved was acquired by some past illegal act, *Loughran v. Loughran*, 292 U. S. 216, 228, and where an agreement has been executed, completed—is at an end—when the illegal transaction has been consummated and property rights have vested, subsequent rights will not be denied because of illegality in their acquisition. *Brooks v. Martin*, 69 U. S. 70; *Planters' Bank v. Union Bank*, 83 U. S. 483; *National Bank & Loan Co. v. Petrie*, 189 U. S. 423; *United States Express Co. v. Lucas*, 36 Ind. 361; *Judson v. Buckley*,

130 F. 2d 174, and *Union Pac. R. R. Co. v. Durant*, 95 U. S. 576.

"In *United States Express Co. v. Lucas*, 36 Ind. 361, the court said:

> 'If money * * * (has) been actually paid to an agent for the use of his principal, the legality of the transaction, of which it is the fruit, does not affect the right of the principal to recover it out of the agent's hands. For though the law would not have assisted the principal, by enforcing the recovery of it from the party by whom it was paid, because it is the policy of the law not to aid the completion of an illegal contract, yet, when that contract is at an end, the agent, whose liability arises solely from the fact of having received money for another's use, can have no pretense to retain it.'
>
> '* * * If money due to a principal on an illegal transaction should be paid over to his agent for him by the party from whom it is due, it has been held that the principal may recover it from the agent; for the contract of the agent to pay the money to his principal is not immediately connected with the illegal transaction; but it grows out of the receipt of the money for the use of his principal.' p. 369.

"*Brooks v. Martin*, 69 U. S. 70, involved a case in which the parties had entered into a partnership contract against public policy. The partners illegally purchased soldiers' rights to land warrants. After realization of the profits, defendant purchased plaintiff's interest in the partnership. Plaintiff, claiming that he was induced to sell his interest in the partnership because of the fraudulent representations of defendant (Brooks) sued to set aside the sale and for an accounting. The court held that recovery could not be defeated by the claim of illegality, and said:

> 'Does it lie in the mouth of the partner who has, by fraudulent means, obtained possession and control of all these funds, to refuse to do equity to his other partners, because of the wrong originally done or intended to the soldier? It is difficult to perceive how the statute, enacted for the benefit of the soldier,

is to be rendered any more effective by leaving all this in the hands of Brooks, instead of requiring him to execute justice as between himself and his partner; or what rule of public morals will be weakened by compelling him to do so? * * * The transactions which were illegal have become accomplished facts, and cannot be affected by any action of the court in this case.' p. 80.

"The party for whom the pipe line in the *McMullen* case, *supra*, was constructed, was a municipal corporation. Thus it affected public rights. The court in that case distinguished *Brooks v. Martin, supra*, as affecting only private rights. In discussing the question the court said:

'The court refuses to enforce such a contract (the contract in the *McMullen* case), and it permits defendant to set up its illegality, not out of any regard for the defendant who sets it up, but only on account of the public interest. It has been often stated in similar cases that the defence is a very dishonest one, * * * and it is only allowed for public considerations in order the better to secure the public against dishonest transactions.' p. 669.

"In our case no public rights are involved. The arrangement pertained to the purchase of property at a public sale which had been widely advertised with a view to selling the securities at the highest possible price. The Van Sweringens, as officers of Vaness and CTB, did not initiate the sale. They could not have prevented it. They had no control over it. *They bid to the limit of the financial backing that they were able to secure.* Their bid was the highest. In this situation, the mere fact that Vaness and CTB had rights which might have been successfully asserted against the Van Sweringens does not of itself enable defendants to escape liability for the conversion of the 8250 shares of stock.

"*Moreover, if we were to accept defendants' contention, we would have to repudiate the basic findings of the court.* We would have to say that Ball and Tomlinson owned all of the common stock of Mid-

> america outright and merely gave the Van Sweringens a conditional option on it for their agreement to render illegal services, so that recovery herein is enforcing such an illegal contract, contrary to public policy. *But the court did not so find.* As we have already stated, the court found as facts, that the parties had entered into a joint venture in which Ball and Tomlinson were to receive forty-five per cent of the profits represented by 45% of the stock of Midamerica, the partnership to receive fifty-five per cent of the profits through its ownership of 55% of the stock; that the partnership performed its part of the agreement, its performance constituting the consideration for their 8250 shares and thereby their interest in the stock was available to them. *Thus, the Van Sweringens, not Ball, owned the 8250 shares. The purpose of the arrangement was fully closed, completed and had come to an end.*" (R. 3052 *et seq.*)

It is clear that the Circuit Court of Appeals did not, as petitioner contends, purport to limit the right of third persons to raise the question of illegality to matters involving public rights. It merely pointed out that this Court in *McMullen v. Hoffman,* distinguished *Brooks v. Martin,* 69 U. S. 70, on the ground that it involved only private rights, and that this case also involves only private rights. This Court said in the *McMullen* case (174 U. S. at p. 668):

> "There is a difference between the case before us and that of *Brooks v. Martin,* because in the latter case the fact existed that the transactions, in regard to which the cause of action was based, were not fraudulent and they related in some sense to private matters, while in the case before the court the entire contract was a fraud and was illegal, and related to a public letting by a municipal corporation for work involving a large amount of money, and in which the whole municipality was vitally interested."

In the discussion of the *Brooks* case it was further said (p. 668):

"The action was sustained upon the theory that the purpose of the partnership agreement had been fully closed and completed; substantially all the profits arising therefrom had been invested in other securities, or in lands, and that therefore *it did not lie in the mouth of the partner who had* by fraudulent means *obtained possession and control of these funds to say to the other that the original contract was illegal.* The wrong originally done or intended to the soldier *had been wiped out by the acts of the soldier* and *his waiver of any claim by reason of the illegal contract.* The transactions which were illegal, the court said, had become accomplished facts, and could not be affected by any action which the court might take."

It is equally true here that any wrong done to Vaness or C.T.B. must be deemed an accomplished fact also wiped out by the settlement and extinguishment of their claims. Here also the purpose of the arrangement had been fully closed and completed long before any assertion of illegality was ever made, and long after the certificates would have been issued outright except for the willingness of Ball and Tomlinson to cooperate in aiding the Van Sweringens to defraud their creditors. (Finding 15, R. 2717.)

In the *McMullen* case this Court further said (p. 667):

"We must take the whole agreement, and remember that the action is between the original parties to it; that there is no collateral contract and no new consideration and no liability of a third person."

The principle stated by the Circuit Court of Appeals that where an agreement has been executed, the illegal transaction has been consummated, and property rights have vested, subsequent rights will not be denied because of illegality in their acquisition, was recognized and applied by this Court long before the *McMullen* case (*Brooks v. Martin,* 69 U. S. 70, *Union Pac. R. Co. v. Durant,* 95 U. S. 576), as well as since that decision (*Loughran v. Loughran,* 292 U. S. 216, 228). That principle did not apply to the

McMullen case *where recovery on an executory contract was sought.* It is fully applicable and was properly applied here.

Petitioner argues that the arrangements between Ball and Tomlinson and the Van Sweringen partnership were never fully executed, because the stock certificates were never issued to the Van Sweringens, and that the authorities with reference to consummated transactions are therefore inapplicable. In this they confuse the steps that were taken in fully carrying out the arrangement, with the situation which arose by reason of Ball's subsequent conversion of the Van Sweringen stock. The agreement was fully performed when Midamerica bought the property at the Morgan sale and the Van Sweringens went into control. The mere fact that certificates evidencing ownership were not issued did not leave the transaction executory. Ball presumably did not become the owner of his stock for the first time when the certificates for his 45% were issued. Nor was the issuance of certificates necessary to the ownership of the Van Sweringens. They were in a position to and under the findings had the right to issue the certificates whenever they pleased. Issuance was deferred only because of the claims of creditors. The factual situation in this respect is wholly different from that in *McMullen v. Hoffman.*

Obviously if the Van Sweringens had actually issued the certificates to themselves and Ball had purloined them after the death of O. P. Van Sweringen, no court would entertain illegality in their acquisition as a defense. No different principle applies here. The situation is similar to that in *Union Pac. R. Co. v. Durant,* 95 U. S. 576, 24 L. Ed. 391, where an action was brought by the railway company to require the defendant to convey certain lands which had been deeded to him. In most of the deeds he was designated as trustee, although one was to him individually, and none of the deeds disclosed the character or

beneficiary of the trust. It was held that the trust could be established by parol and that illegality of the transaction between the grantors and the railway company was no defense. The following language is pertinent:

> *"The conveyances to the trustee, were in the view of the law, the same thing as if they had been to the company. The transaction between the parties in interest was thus finally closed.* There will be neither more nor less of illegality between the original parties, whether the trustee does or does not respond to his obligation to the company. In that obligation there is no pretence for saying there is any taint of any kind; and it is that obligation alone which it is sought to enforce by this proceeding. * * * The appellee cannot claim adversely to those for whom he acquired and holds the property. *The rights of others, if such rights exist, do not concern him. He cannot vicariously assert them.*
>
> "The office of a trustee is important to the community at large, and frequently most so to those least able to take care of themselves. It is one of confidence. The law regards the incumbent with jealous scrutiny, and frowns sternly at the slightest attempt to pervert his powers and duties for his own benefit. The tenant cannot deny the title of his landlord. *A multo fortiori* ought not the trustee to be permitted to deny that of his beneficiary.
>
> * * * * *
>
> *"The conduct of the appellee, stripped of the verbiage with which it has been surrounded, and viewed in its nakedness, strongly offends the moral sense of the judicial mind."*

No apter language can be found to describe the contention of the petitioner here than the concluding sentence of the foregoing opinion. The result in this case in no way conflicts with *McMullen v. Hoffman*, or with any recognized principle of federal or state public policy.

a. No Question of Illegality Remained After the Settlements with Vaness And C. T. B.

In discussing the principles relating to illegality and public policy, petitioner has failed to take into account the Vaness and C.T.B. settlements by which all claims of such corporations were fully compromised and satisfied with approval of the respective courts in which the affairs of such corporations were then being administered. With reference to these settlements the Circuit Court of Appeals said:

> "We think our conclusion is fortified by the fact that representatives of the proper parties to complain of the Van Sweringens' breach of fiduciary duty—Vaness, CTB, their stockholders and creditors—instituted actions against them. These actions were settled. After reading the comprehensive terms of the settlements which appear in the record, we are convinced that the court correctly found that there had been full satisfaction of any claims that the proper parties may have had against Midamerica, Ball, and Foundation because of the asserted violation of fiduciary duty owed by the Van Sweringens, personally, or the partnership, in the sale and purchase of the securities in Groups 1 and 3 at the Morgan sale. Although defendants assert that because they limited the releases to themselves, in the settlements which they made, Vaness and CTB have never sanctioned the conduct of the Van Sweringens, their assertion is untenable. When those companies compromised their claims, they necessarily confirmed the title of Midamerica therein, so defendants may not now be heard to complain that their rights had been violated."

Illegality of an agreement resulting from a contemplated breach of fiduciary obligations or from a tendency to result in such violations, unlike other types of illegality may be eliminated by ratification by the principal or beneficiary.

Restatement, Contracts, Sec. 570;
Restatement, Restitution, Sec. 191;
Williston on Contracts (Rev. Ed.) Vol. 6, Sec. 1737;

Cogswell Lumber Co. v. Manahan, 135 Okla. 174, 274 Pac. 871.

In Vol. 6 *Williston on Contracts* (Rev. ed.) Sec. 1737 the author states that:

> "While it would seem that a bargain which has been declared void as contrary to public policy should be incapable of validation by any private person the law is otherwise with respect to these bargains of a fiduciary *which may be vadidated by the effective consent of the beneficiary or principal."*

No more effective consent or ratification could conceivably be given than where as here the principals have, for a consideration acceptable to them, compromised all claims based on the asserted breach of fiduciary relations.

This principle is fully applicable here and is a complete additional answer to petitioner's contention.

b. A Third Person Cannot Assert Violation of a Fiduciary Obligation as a Defense Where No Moral Turpitude or Actual Fraud is Involved.

The District Court found and the Circuit Court of Appeals specifically stated that no fraud on the part of the Van Sweringens was involved. Where the illegality asserted is a violation of a fiduciary obligation of a corporate officer not involving actual fraud or moral turpitude, a third person can obtain no advantage therefrom.

Deeds v. Gilmer, 162 Va. 157, 174 S. E. 37;
Richardson v. Welch, 47 Mich. 309, 11 N. W. 172;
Robison v. McCracken, 52 Fed. 726.

These authorities are applicable here.

c. Under Indiana Decisions an Agreement Otherwise Legal Is Not Rendered Illegal or Unenforceable Because of Illegal Acts in Performing It.

There is no finding by the District Court or the Master that the agreement between the Van Sweringens and Ball either required or contemplated any breach of fiduciary obligation to Vaness or C.T.B. It was merely an agreement to enter into a joint venture to organize a new corporation to bid for and if possible acquire a portion of the collateral to be sold.

Neither Vaness nor C.T.B. could bid for the collateral and the fact that the Van Sweringens were officers and directors of such companies did not alone disqualify them from bidding at a public sale which they could not prevent and did not control.

McKittrick v. Arkansas Cost. R. Co., 152 U. S. 473, 497, 38 L. Ed. 518, 527;
Allen v. Gillette, 127 U. S. 589, 596;
Vol. 3, *Fletcher on Corporations*, pp. 191, 192.

The fact that they had personally guaranteed the loans which were being foreclosed by Morgan gave them an additional, special right to bid at the sale to protect their own interests on their guaranty. (*Ante*, p. 21.)

As stated by the Circuit Court of Appeals failure to observe strictly their fiduciary obligations in the course of the sale would of course give the corporations a right to complain, but would not of itself affect the validity of their arrangement with Ball. (R. 3055.)

Hogston v. Bell, 185 Ind. 536, involved an action to recover for services claimed to have been rendered in an illegal manner. There it was held—(1) that a contract is not void as against public policy unless it requires that something be done which adversely affects the public welfare or is forbidden by law, or unless its consideration is illegal or immoral; (2) that where a contract is capable of being performed in a legal manner, the mere fact that one

party thereto performed it in an illegal manner will not render it illegal; (3) that if a contract is legal in its nature and one which the parties had a right to make, it cannot be rendered invalid by the fact that in its performance one of the parties could or might employ improper means or agencies. In *Phend v. Midwest Engineering, etc. Co.*, 193 Ind. App. 165, the court briefly summarized the rule as follows:

> "All the provisions of the original contract could have been performed in a legal manner. The several provisions of the original contract being valid, they will not be declared void because some of them were partly performed in an illegal manner."
>
> See also *Russell v. Burton* (N. Y.), 66 Barb. 539.

d. Respondent's Status as Transferee and Representative of Creditors.

The Circuit Court of Appeals assumed for the purpose of the decision that respondent occupied the same position as the Van Sweringens. This Court, however, in *McMullen v. Hoffman, supra,* took occasion to state that it should be remembered that that action was between the original parties.

In *Hutchins v. Weldin,* 114 Ind. 80, the Supreme Court of Indiana approved an instruction containing the following language:

> "One qualification of the rule (the illegality rule) is, that the rule itself shall not be made an engine of wrong and injury in the hands of a wrong-doer against an innocent party. It can never be good policy to punish the innocent for the crimes of the guilty; hence the rule can not be set up to the prejudice of any party innocent of all participation in the wrong or whose rights have been acquired without notice of it * * *."

Even illegal transactions are not nullities and may create rights. Courts usually refuse to assist in the enforcement

of such rights, not because the rights are non-existent, but because on grounds of public policy the judicial machinery ought not to be permitted to be used by a participant. The rule stated by *Williston*, Vol. V, Sect. 1630, is that *"Where relief is denied it is either because the plaintiff is a wrong doer and such person as the law does not aid, or in exceptional cases, because the transaction is declared absolutely void by statute."*

In considering the defense of illegality in *McMullen v. Hoffman, supra,* this Court said:

> "It has been often stated in similar cases that *the defense is a very dishonest one,* and it lies ill in the mouth of the defendant to allege it, and it is only allowed for public considerations and in order the better to secure the public against dishonest transactions."

We submit that no "public considerations" compel the application of the principle here where an innocent transferee, with no notice of any claim of illegality, is merely attempting to obtain for innocent creditors the value of converted property which would have been available to them in 1935 except for the scheme to defraud them in which petitioner himself participated.

e. The Decision of the Circuit Court of Appeals Is Not in Conflict With In Re Van Sweringen Co. (C. C. A. 6) 119 F. 2d 231.

The decision in this case recognizes the right of Vaness and C.T.B. to complain of any violation of the fiduciary obligations of the Van Sweringens to them, at any time prior to the settlement of their claims. It holds, however, that Ball cannot evade his liability for conversion by asserting the rights of, or wrongs to, these corporations. The case of *In re Van Sweringen,* 119 F. 2d 231, involved the assertion of such rights by the corporations themselves prior to the settlement, and did not involve the validity of the agreement between the Van Sweringens and Ball. Thus the

cases not only do not conflict but are in complete harmony, as the Circuit Court of Appeals in this case said:

> "Defendants also argue that there is an inconsistency between the court's decision and that of the court in *In Re The Van Sweringen Company,* 119 F. 2d 231, where Midamerica was allowed to prove obligations of the Van Sweringen subsidiaries purchased at the Morgan auction only in the amount actually paid therefor. But there is a fundamental difference between that case and the present cases. There, the subsidiary corporations themselves were seeking to protect their own rights, whereas here defendants are seeking to use, solely for their own benefit, whatever rights Vaness and CTB may have had at one time, even though such rights have now been extinguished by the settlements with Foundation." (R. 3056, 3057.)

It may also be noted that the companies whose notes were involved did not in the earlier case question Midamerica's title to such notes. They merely denied its right to prove in bankruptcy the full face amount of the notes which had been purchased by it for a nominal price. The breach of fiduciary obligation involved there was the obligation to give the corporation the benefit of a cheap purchase, not the obligation to abstain from purchasing. Both cases were correctly decided on their facts.

f. There is no Conflict with State Decisions.

Even a cursory examination of the decisions cited by petitioner as in conflict with this decision demonstrates their inapplicability.

In *Thomas v. Mathews,* 94 O. S. 32, the court simply declined to enforce a personal contract of a single director to cause his company to pay certain dividends.

The Indiana cases which relate to corporate officers all involve directly relations between the offending officer and the offended company.

In *Overshiner v. Wisehart*, 59 Ind. 135, the plaintiff was held not entitled to recover on a note executed to cheat a third person by making him believe that a falsely pretended transaction between the maker and payee was genuine.

In *Western Union Telegraph Company v. Yopst*, 118 Ind. 248, it was held that in order to recover a statutory penalty in connection with a telegram sent on Sunday it was necessary to prove a necessity for sending it on that day in view of the statute prohibiting the transaction of business on Sunday.

No comment on these cases is required. The decisions of other states cited by petitioner are equally remote from any question involved in this case. The opinion of the Circuit Court of Appeals makes a proper disposition of the question of illegality on the facts of this case, and does not conflict with any applicable decision of this Court or any state court.

C. ESTOPPEL.

The facts on which the claim of quasi estoppel is based are set forth in respondent's Statement of the Case (*ante* pp. 10-11).

With reference to the applicability of the doctrine here the Circuit Court of Appeals said:

> "This contention is based on the fact that in 1937 Midland, one of the four Cleveland banks for whom plaintiff sues, sold to Foundation 754½ shares of Midamerica common stock at a profit of $523,000, upon the theory that all the rights of the Van Sweringens in respect to the stock had terminated. The claim is made that the other three Cleveland banks approved or ratified this action of Midland, and derived financial benefit from it because they were obligated to make up the deficiency between the liabilities and the assets when the insolvency proceedings of Midland were wound up, so that by this profit their obligation was

reduced *pro tanto*. Defendants argue that having benefited from the sale of the stock on the theory that the partnership had no rights therein, plaintiff should not now be allowed to assert that the partnership did have such rights.

"The following facts must be borne in mind in considering defendants' contention. Ball knew that Tomlinson had transferred his stock to Midland. He had given his consent thereto. The negotiations for the purchase of the stock from Midland were not begun until after Ball had converted the stock by transferring 14,050 shares of Midamerica to Foundation and had parted with all personal interest therein. The negotiations for the purchase of the stock from Midland were not concluded until Foundation had sold at least 93% of Midamerica stock to Young, Kolbe and Kirby for more than six million dollars. Thus Ball knew all the facts insofar as Midland was concerned, and he was not influenced in any manner by any representation or act as to the ownership of the stock made by Midland or the other three Cleveland banks. The Cleveland banks made no representations concerning their interest in the proceeds of the sale, nor did they conceal their interest in Midland's affairs.

"During all the negotiations the facts with reference to the ownership of the stock were well known to Ball, as well as to Foundation. Mr. Cox, in charge of the liquidation of the Union Trust Company, and the liquidator of the Guardian Trust, as creditors of the Van Sweringen partnership, made demands on Ball for the protection of the Van Sweringens' interest in Midamerica within a few days after O. P. Van Sweringen's death. These were followed by further conferences, by formal written demand in early February, 1937, and by the formal written demand, on April 1, 1937, of the receiver of the Van Sweringen partnership. In view of such continuing demands to and at the very time of the conversion, the contention that Ball was in some way prejudiced or misled by Foundation's subsequent unconditional purchase of the Midland stock is clearly without merit. When Ball con-

verted the stock on April 1, 1937, thus repudiating all claims of the partnership receiver with reference thereto, he could not have, and does not claim to have, relied on any action of Midland or any other creditor of the Van Sweringens. The same thing is true as to the conversion by Foundation. By those acts Ball and Foundation assumed full responsibility for any liability that arose as a result. Neither Midland nor any other creditor of the Van Sweringens knew any facts with reference to the title to such stock that Ball himself did not know. Neither Midland nor anyone else made any representations to Ball as to the status of the claim for conversion which had already accrued or as to any effect thereof on the ownership of Midland's Midamerica stock, and there is no basis in the transaction for implying any representation to Ball or Foundation that the consequences of the original wrong would be obviated by the purchase of Midland's stock.

"In order to have an estoppel, there must be a representation or concealment of material facts; the representation must have been made with knowledge of the facts; the party to whom the representation was made must have been ignorant of the truth of the matter; the representations must have been made with the intention of inducing the other party to act; and the other party must in fact have acted thereon. *Kerestury v. Elkhart Packing Co.*, 108 Ind. App. 148, 153; *Weber v. Fohl*, 111 Ind. App. 388, 394; *Damler v. Baine*, 51 N. E. 2d 885, 889; *Lebold v. Inland Steel Co.*, 125 F. 2d 369, 375. Virtually all the elements of equitable estoppel are lacking here. Certainly there is no showing that Ball was induced to act by any representations and then acted in reliance thereon, or that Ball was ignorant of the situation. From the foregoing it is apparent that the doctrine of equitable estoppel has no application here.

"The proper function of equitable estoppel is the prevention of fraud, actual or constructive, and the doctrine should always be so applied as to promote the ends of justice and accomplish that which ought to be

done between man and man. 19 *Am. Jur.* pp. 637-8. It should not be diverted or turned from its proper end into an instrument of wrong, which would result here if plaintiff were held estopped. Since Ball and Foundation knew all the facts, it would be inequitable to hold that because Foundation bought Midland's interest at a substantial profit to Midland and the other banks ultimately received a benefit therefrom, there was a termination of their right to recover ten times the proportionate amount paid by Foundation for 55% of Midland's Midamerica stock. This equitable doctrine should not be applied to benefit a converter by permitting retention of the fruits of the conversion.

"*Recognizing that equitable estoppel is inapplicable here, defendants invoke the doctrine of quasi estoppel* in which reliance upon the part of the one asserting the estoppel is not necessary. Thus defendants point out that by ratifying and benefiting from Midland's sale of the 754½ shares free from any rights of the receiver, Midland elected to treat those rights as terminated and is estopped to say otherwise. As to Midland, defendants' position is sound, so 55% of the amount paid for Midland's Midamerica stock must be deducted from the recovery.

"But defendants seek far too broad an interpretation and application of the doctrine of quasi estoppel when they attempt to use it to block the other creditors' right to recover. At the most, the Cleveland banks merely received a part of their own money from their benefit from Midland's sale. It is well settled that even by quasi estoppel one cannot be estopped by reason of accepting that which he is legally entitled to receive in any event. 31 *C. J. S.* p. 350, n. 23. Here, the Cleveland banks were entitled to receive the proceeds or damages for the conversion of 8250 shares of Midamerica common stock. Defendants' claim, at best is that the beneficiaries of plaintiff's trust have received the proceeds of 414.975 shares of such stock. They have never received anything on any theory for the remaining 7,835.025 shares. Since this doctrine operates as a shield, not as a sword, 19 *Am. Jur.* p. 639, it

should not be applied beyond what is necessary to accomplish justice between the parties and so does not extend beyond the damage sustained by Ball. 19 *Am. Jur.* p. 640. Hence 55% of the amount paid for Midland's Midamerica common stock (plus legal interest thereon) must be deducted from the recovery." (R. 3057-3060.)

In denying a rehearing that court further said:

"Petitioners argue that full effect has not been given to the doctrine of estoppel. True, the result reached is akin to that of set-off. But that does not indicate that there has been an erroneous application of the doctrine of quasi estoppel. For that doctrine is essentially one of fundamental justice which must be so applied as to reach the fairest possible result in the particular circumstances. In our case, Ball paid Midland for its Midamerica stock, and should not be forced to pay for it again by including it in the recovery. Clearly, the extent that Ball was damaged was the amount that he paid for fifty-five per cent of Midland's Midamerica common stock, so this amount should, and will, be deducted from the recovery." (R. 3072.)

Petitioner contends that by failing to deny recovery entirely the court failed to follow applicable Indiana decisions. The two cases cited in support of the contention are obviously inapplicable to anything involved here.

In *Maxon v. Lane,* 124 Ind. 592, it is held that if a party who holds a mortgage declares it to be invalid or agrees not to enforce it, or makes representations or does acts whereby another is induced to change his position and expends money, he is estopped by such representations and acts whether fraudulent or not, to foreclose the mortgage. No such question is involved here and no question as to whether the doctrine of estoppel or quasi estoppel extends beyond the damage claimed to have been sustained was presented in that case.

In *Wilmore v. Stetler,* 137 Ind. 127, a guardian of an insane ward sold as her absolute property land in which

she owned only a one-third interest, her children owning the balance. After coming of age the heirs with full knowledge of their interest in the real estate accepted the proceeds and thereafter sought to quiet title to their two-thirds. It was held that they could not at the same time retain the money and assert their title to the property.

That estoppel *in pais* never extends beyond the damage actually sustained by the party asserting it, is a well settled doctrine of this Court. In *Baker v. Wood*, 157 U. S. 212, 39 L. Ed. 677, it was said:

> "The doctrine invoked is purely equitable and ought not to be extended, under circumstances like these, beyond permitting the person misled to recover indemnification."

To the same effect are:

Payne v. Bursham et al., 62 N. Y. 69, 74;
Campbell v. Nichols, 33 N. J. L. 81, 88.

In 19 *Am. Jur.* 640, the principle is stated as follows:

> "Since as has already been stated, estoppel *in pais* operates as a shield and not as a sword, the estoppel should not be given effect beyond the extent of the injury or beyond what is necessary to accomplish justice between the parties but should be limited to saving or making whole the person in whose favor it arises or in other words to what may be necessary to put the parties in the same relative position which they would have occupied if the predicate of the estoppel had never existed."

There is no reason why any different principle should apply to quasi estoppel, and no Indiana decision which in any way impinges on such principle. If the doctrine of quasi estoppel is applicable to the Midland sale as the Circuit Court of Appeals has held, certainly the result reached fully accords with the foregoing principle.

The statements in petitioner's brief (pages 26-27), to the effect that the four Cleveland banks "either actively participated in the sale by Midland to petitioner or ap-

proved and ratified the transaction * * *" and "were equal participants in the sale of Midamerica stock to petitioner * * *", are simply not supported by any finding or evidence in the record. As heretofore pointed out, the Guardian and Union were in liquidation with the state officers and were denying any obligation in connection with Midland liquidation.

Petitioner has the temerity, in urging this contention, to describe the respondent's position as "unconscionable." Actually, it would be a travesty if the beneficiaries of respondent's trust by having their possible underwriting obligations reduced by the amount paid to Midland for 414.975 shares (to which they were entitled in any event), should be held to have lost their right of recovery for the value of the 8250 shares, leaving petitioner and his family corporation in full possession of the proceeds of their conversion, especially where, as here, the money paid to Midland came from the proceeds of the converted stock. Such a result would indeed be unconscionable.

For the reasons above stated respondent requests that the petition for a writ be denied.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1944.

No. 426.

GEORGE A. BALL,
Petitioner,

vs.

H. EARL COOK,
Superintendent of Banks of the State of Ohio in Charge of the Liquidation of The Union Trust Company, Cleveland, Ohio, Trustee,
Respondent.

PETITIONER'S REPLY BRIEF ON PETITION FOR WRIT OF CERTIORARI.

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This reply brief is addressed solely to respondent's contention that he does not rely, in support of his claim, upon activities of Van Sweringens which were found to have been in violation of their fiduciary duties to C.T.B. and Vaness.* That Van Sweringens violated their fiduciary duties to C.T.B. and Vaness in connection with the Morgan sale cannot be questioned, for the Special Master, the District Court and the Circuit Court of Appeals have all so held. (R. 2847-2849, 2898-2900, 3055, 3056.)

* In his main brief petitioner accurately and adequately stated the facts material for a consideration by the Court of the questions presented in the petition for writ of certiorari. In the restatement of the facts in respondent's answer brief there is a statement to the effect that "a similar plan was prepared for and taken by them (the Van Sweringens) to their first meeting with Ball three days later" (p. 4). Ball never saw or knew of this plan or any of the other plans of Van Sweringens until about the time of the trial of this case; and whatever plans Van Sweringens may have had with them at their first meeting with Ball, they were never shown to him. This is established by undisputed evidence. (R. 470, 471, 524, 525.)

In the District Court respondent was faced with the fact that his predecessor in interest—the Van Sweringen partnership—had not invested a dollar in Midamerica and that the written contract gave only an option to buy Midamerica stock on conditions which were never met. Respondent therefore tried his case on the theory that Van Sweringens, by reason of their unusual relationship to Morgan and to the collateral pledged by C.T.B. and Vaness, were able to and did procure for Midamerica a bargain purchase so great as to compel the inference that Van Sweringens were entitled to (and therefore that the agreement must be deemed in substance that they should have) ownership of 8250 shares of Midamerica, and that in consequence the condition precedent to the exercise of the option was in fraud of their creditors.

In support of this theory respondent introduced evidence that the securities purchased by Midamerica at the Morgan sale had a fair and reasonable value on the date of purchase which exceeded the price paid for them by more than $2,000,000 (R. 353-355; 395-396) and he convinced the trial court that Van Sweringens thereby had brought to Midamerica a bargain purchase "for which they were entitled to compensation." (Finding No. 17, R. 2720.) Faced on appeal and on the petition in this Court with the finding that in bringing a bargain purchase to Midamerica Van Sweringens had violated their fiduciary duties to C.T.B. and Vaness, respondent has abandoned the theory on which he obtained his judgment in the trial court and now boldly asserts that Van Sweringens' right to 8250 shares of Midamerica stock was not and is not an issue in the case.

Petitioner did not introduce the evidence on which the finding of a breach of fiduciary duty was based. That evidence was introduced by respondent as an essential part of his case in an effort to show the substantial consideration furnished by the Van Sweringens, to wit, their services,

arrangements and relationships, in connection with the acquisition by Midamerica of the collateral owned by C.T.B. and Vaness. If, as claimed by respondent (in invoking the doctrine of *Brooks v. Martin*, 69 U. S. 70; *Loughran v. Loughran*, 292 U. S. 216 and related cases) the illegality was a thing of the past and wholly unrelated to the present case, then the evidence of that illegality would not have been introduced by respondent. *But that evidence was introduced and relied upon by respondent* and his claim is therefore clearly within the doctrine of *McMullin v. Hoffman*, 174 U. S. 639.

The complaint (R. 1) and the opinion of the District Court (R. 2725) clearly show respondent's reliance and dependence upon the activities of Van Sweringens which have been found to be violative of their fiduciary duties to C.T.B. and Vaness.

The first count of respondent's complaint (incorporated by reference into all the other counts) alleged that J. P. Morgan & Co. and associates wanted to have Van Sweringens continue in the control of their "empire" (Par. 14); that the plans for Van Sweringens to retain control of the "empire" were facilitated by the manner in which the collateral was grouped for sale (Par. 16); that when the financing of the purchase of the collateral by Ball and Tomlinson had been secured by Van Sweringens, they advised Morgan who shortly thereafter gave due notice of intention to sell the collateral (Par. 19); that at the sale Van Sweringens caused the collateral to be purchased for Midamerica for $3,121,000 and that such collateral then had "*fair or reasonable market value*" of $6,455,101.62 (Par. 26 and Ex. 7 thereto); that by procuring for Midamerica the opportunity to acquire at said price said assets of such large value, Van Sweringens brought and contributed to Midamerica assets and services of a net value to Midamerica (*exclusive of control value*) substantially in excess of $3,300,000 and for such contribution

they became entitled then and there to the ownership and control of 8250 shares of Midamerica common (Par. 27); that said 8250 shares had an actual value in excess of $1,800,000 by reason of the great value of the services furnished and contributed by Van Sweringens (Par. 28); that the consideration for the 8250 shares "was the services, arrangements and commitments" furnished by Van Sweringens (Par. 28). Respondent offered evidence in respect of all of these averments.

Thus respondent relied on the right of Van Sweringens to the 8250 shares in consideration of their services and arrangements in procuring a bargain purchase of C.T.B. and Vaness collateral for Midamerica and this was the basis of respondent's claim that the option agreement was in fraud of Van Sweringens' creditors.

The opinion of the District Court clearly shows the essential nature of respondent's claim in that court:

> "It is the contention of plaintiff that the Van Sweringens not only called to the attention of defendant and Tomlinson the investment opportunity involved in the auction sale of Groups 1 and 3 on September 30, as stated in the letter of September 21, but also, through their position, relationship and activities leading up to the sale, furnished considerations which *were the moving, effecting force in bringing to and securing for the defendant, and for Midamerica Corporation, the bargain purchases of such groups of securities;* that such bargain purchases were of great value to the defendant, and to Midamerica Corporation; that the plan and arrangement, as set forth in the letter of September 21, whereby it sought to limit the rights and interests of the Van Sweringens in fifty-five per cent (55%) of the common stock of Midamerica Corporation so that such stock could not be reached by their creditors, was an effort to hinder and delay such creditors, and, therefore, constituted a fraud upon them and are invalid. * * * On the other hand, it is the contention of the defendant that the Van Sweringens furnished no considerations which were the moving, effecting

force in bringing to and securing for the Midamerica Corporation the bargain purchase of Groups 1 and 3 of the securities sold at the auction sale on September 30. * * *" (R. 2740, 2741, emphasis supplied).

Thus the real issue in the trial court was whether the Van Sweringens had brought to Midamerica a bargain purchase of the C.T.B. and Vaness collateral entitling them to ownership of the 8250 shares.

Findings Nos. 16 and 17 (R. 2718-2720) clearly disclose that the court found that Van Sweringens by reason of their relationship to J. P. Morgan & Co. and of their arrangements and activities in connection with the sale of the C.T.B. and Vaness collateral, brought a bargain purchase to Midamerica and that these services were the sole consideration furnished by them for the 8250 shares in controversy. These two findings, which are the basic findings of the trial court, establish the complete dependence of respondent's claim upon the right of Van Sweringens to the 8250 shares *as compensation for the very services which were indisputably in violation of fiduciary duty.* On the basis of these services respondent has obtained a judgment which, with interest, amounts to approximately $4,000,000.

It makes no difference what form the action takes. Claims based on conversion, tort, replevin or to enforce a resulting trust have all been condemned as illegal and unenforceable where, as a part of the plaintiff's case, he has been required to prove and rely upon arrangements or activities condemned by law.[1] There can be no doubt of the fact that the law condemns the activities of dominant directors who use their position and relationships or "their

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[1] *Flegenheimer v. Brogan*, 284 N. Y. 268, 30 N. E. (2) 591 (1940); *Meyers, et al. v. Henderson*, 204 Ind. 104, 181 N. E. 729 (1932); *Hutchins v. Weldin*, 114 Ind. 80, 15 N. E. 804 (1888); *Smith v. Barnes*, 129 Ore. 138, 276 Pac. 1086 (1929). See also *American Locomotive Co. v. Histed*, 18 F. (2) 652, 656 (D. C. Mo., 1926).

negotiating skill and business acumen'' to obtain a bargain purchase of the assets of their companies upon foreclosure —and particularly when millions of dollars of bonds and other securities of those companies are widely scattered in the hands of the public.

That respondent's claim is based fundamentally upon the activities of Van Sweringens in clear violation of their fiduciary duties is inescapable and no language or argument can obscure this basic fact.

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